



**EVA VAN LENTEREN EUROPEAN STARTUPS IN THE CHINESE MARKET:
WHAT ARE THE FIRST IMPORTANT STEPS?**

**STARTUPS EUROPEIAS NO MERCADO CHINÊS:
QUAIS SÃO OS PASSOS PRIORITÁRIOS?**



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WHAT ARE THE FIRST IMPORTANT STEPS?**

Dissertation presented to the University of Aveiro to comply with the requirements for obtaining the Master's degree in Estudos Chineses, carried out under the scientific guidance of Dr. Professor Álvaro Augusto da Rosa, Auxiliary Professor, Marketing Department, Operations and General Management of IBS, ISCTE-IUL.

To my parents, my aunt and stepmother who all helped me find my 'caminho' and supported me unconditionally while searching for it.

o júri

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keywords

China; Portugal; Startups; Investment Vehicles; WFOE; Joint Venture; Guanxi

abstract

In this thesis, which I write as a final work for the master in Chinese Studies at the University of Aveiro, I will research Portuguese Startup companies, the interest they have in entering the Chinese market and the difficulties they might come across when doing so. I will investigate their investment vehicle, their product and the barriers they have setting up their company and negotiating with the Chinese. I will make a questionnaire to obtain the right information and will draw my conclusions after having investigated these issues. I will try to come up with a plan to help them and to see how they can be facilitated with overbridging language and culture differences. And how I specifically, can help with the knowledge gained throughout my studies.

palavras-chave

China; Portugal; Startups; Veículos de Investimento; WFOE; Joint Venture; Guanxi

resumo

Nesta tese, que desenvolvo como trabalho final do mestrado em Estudos Chineses, farei uma pesquisa sobre empresas portuguesas Startups, o interesse que têm no mercado chinês e as dificuldades que poderão encontrar no seu percurso de introdução neste mercado. Procurarei obter informação sobre os seus meios de investimento, produtos e dificuldades nas negociações. Elaborarei um questionário para obter a correta informação e apresentarei as conclusões depois de estudar as respostas apresentadas. Procurarei apresentar um plano para ajudar estas empresas a ultrapassarem os problemas criados pelas diferenças de língua e cultura com o objetivo de as auxiliar pondo em prática o conhecimento que adquiri ao longo dos meus estudos.



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List of Abbreviations

UHP – UrHome Portugal, Real Estate Agency

WFOE – Wholly Foreign Owned Enterprise

JV – Joint Venture

RO – Representative Office

WTO – World Trade Organization

AoA – Articles of Association

EJV – Equity Joint Venture

CJV – Cooperative Joint Venture

HK ltd. – Hong Kong Limited

AIC – Administration for Industry and Commerce

ICBC – Industrial and Commercial Bank of China

Introduction

For a large amount of people (not Chinese), China still is a quite unknown area. Most people do not even know the name of the current Chinese president, never mind the previous president. Or they call him Jinping, because they think that that is Xi's last name (Putten, J. van der, 2011). People do know the president from the United States of America, even though there are four times less Americans than there are Chinese. Our ignorance about the upcoming, or better said returning world power China is quite understandable. China has been isolated from the outside world for a long time, or seen from China's perspective: the outside world has been isolated for a long time from China. The Middle Kingdom could only count on a broader interest from the West when it seemed to be ready for the status of profitable market. The international capital keeps finding its way to China. In 2010 that was 10 billion dollars, therefore the total of international investment reached up to 106 billion dollars (Putten, J. van der, 2011).

But the royal treatment of the international companies by China is over. Nowadays their bosses complain about the new bureaucratic obstacles, unpredictable applications of laws and rules and straight out discriminating measures on behalf of national companies. One example, of many, is that China did not, in conflict with the agreements made when accessing the World Trade Organization (WTO), open its petroleum- nor its telephone market for foreign capitals (Putten, J. van der, 2011). The Foreign investors are somewhat indignant about the rule that the Chinese government



Figure 1 – Investing in China, 2011; Source AFP

developed technology. They see this as a method to force them to tell all about the knowhow to the Chinese. It would be a more elegant version of the old Chinese habit to copy foreign technology where after they would make fake versions of the products and selling these for a lower price (Putten, J. van der, 2011).

How does China work?

China has been charged of constituting obstacles for foreign countries, stealing their technology and duplicating practically everything, even entire stores, such as: Starbucks and Apple. China practically monopolizes through state banks the granting of credits and determines interest, the state banks are poorly integrated in the international financial system, they give cheap credits to Chinese companies and to foreign buyers of Chinese products, they finance on the expenses of the government all Chinese mega projects abroad, China keeps its coin's value low and drives growth towards its export, and in general always thinks about itself before it thinks of the game rules (Putten, Jan van der, 2011).

Almost 70 percent of the 1.8 million Chinese Private Companies has a governmental organization within their walls – it's actually even mandatory – but often these parties were half a sleep. This, however, is changing in rapid tempo, now that chairman Xi Jinping demands that entrepreneurs give priority to 'patriotism', with the party as their 'guide'. A couple large foreign companies later complained to news agency Reuters, about the way that party committee all of the sudden joins the management to discuss strategic decisions about, for example, investments (Vlaskamp, Marije, 2017).

And yet, this is only the beginning. The American newspaper The Wall Street Journal reports that the state is approaching large private internet companies to buy 1 percent of their shares. With result that these companies get a government official in their board of directors. In exchange for this 'special management share', tech-companies get help navigating through governmental bureaucracy. This 1 percent-investment supposedly is optional, but without licenses even the most lucrative internet company in China will not survive (Vlaskamp, Marije, 2017).

Since the beginning of the economic revolution, China needs help from abroad more than ever. Previously it was because of in- and export of merchandise and services and for the delivery of resources, technology and semi-manufactured products. Only after, the abroad became interesting for China as a destination for investment purposes (with one third of the currency reserves of the world in its pocket China seems to have outgrown even itself) and increasingly as food supplier. It seems that the rest of the world is therefore is in service of the development of China as a genuine power. (Horner, Charles, 2009).

Cash Drain

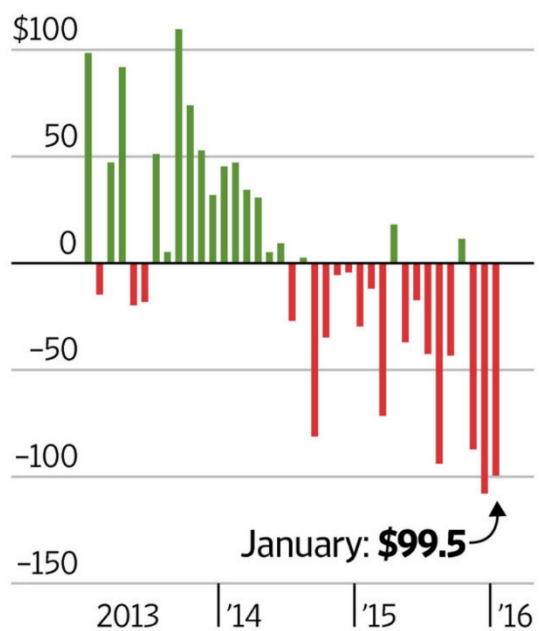
Beijing's interventions to defend the yuan has eaten into the world's largest currency stockpile.

China's foreign reserves, in trillions of dollars



Source: Wind Info

Monthly change, in billions of dollars



THE WALL STREET JOURNAL.

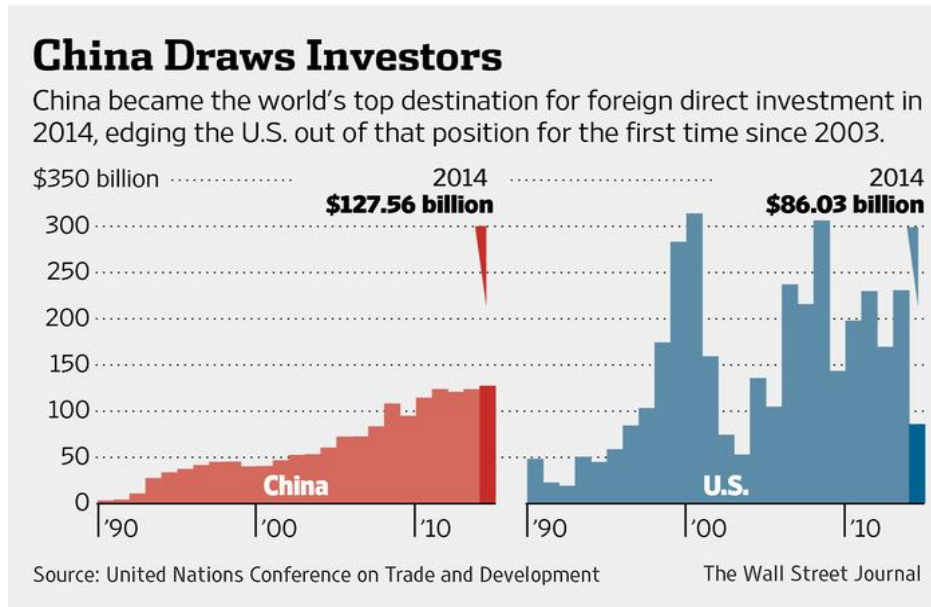
Figure 2 – China's Currency Reserves, 2011; Source Wind Info

Inside China all instruments are present to use foreign companies for own development. One example out of many are the high-speed trains that were built with the Japanese and German technology, copied and further developed. They have a much higher speed and are cheaper to build than the original designs, but also seem to be more dangerous. The joint-venture¹, for many years the only corporate structure for foreign investments, gave the opportunity to the Chinese partner to run off with the by the foreign partner given technologies. The politics of 'national innovation' which is present today, is some more elegant but has mostly the same purpose, which is to transfer of foreign technological knowledge to China in order to develop the economic growth of the country. At the same time the state benefits their own (state) companies. Foreign companies continue being important to China, especially as long as they have technologies which are not yet in China's hands (Putten, Jan van der, 2011).

¹ Joint-venture - a business agreement in which the parties agree to develop, for a finite time, a new entity and new assets by contributing equity.

1. Theory and Dilemma

China attracts more direct foreign investors than other countries. It is the biggest gold rush that has ever taken place. Western business people are almost tripping over each other in their hunt for Chinese gold. (Putten, J. van der, 2006)



But what do they know about China and her Culture? And what do they know about their Culture of negotiation? Europeans and Chinese have very different language and negotiation

techniques, with miscommunication as a result. Figure 3 – China's Gold Rush, 2014; Source: United Nations Conference on Trade and Development

The Chinese do not see negotiation as an instrument to close a deal, they also want to build up a relation with their business partner. This is a gradual process. Western business people have just one objective during negotiations: to reach an agreement as fast as possible. A typical characteristic for this difference in culture is the oftentimes usage of the Chinese word for "support". Culturally seen this key word implies the Chinese definitions for Guanxi (关系, relationship), Nei (内, inner circle) and Wai (外, outer circle). With a request for 'assistance' the Chinese negotiator considers his Western partner as a special member of his own group that is tied to Guanxi (Li, Xiangling, 2009). From the Western negotiator is expected that he supports the Chinese partner. The Chinese tries through this way to build up a relation, he wants to give 'a face to the Western', to reassure him. Also in later stages of negotiation he

will ask his conversation partner nonstop for 'support'. Only then the key word is meant more functional: he asks the negotiating partner to make concessions of a better offer to get to a satisfying outcome. The Western often does not understand the continuously query for support. He assumes as if it were a lack of trust. 'Of course I'll support you. Why don't you trust me? ', is his reaction. They not rarely assume that Chinese have no understanding in modern economical management. Especially the Dutch negotiator, happens to have a pedantic approach. The Chinese is too polite to end this inappropriate way of education as a result that the mutual understanding is being undermined and the negotiations are jammed. Another source of miscommunication (and irritation) is that the Chinese have the urge to tire themselves in extensive background information. The Western negotiation partner might question why the Chinese is telling him all this information, he finds it irrelevant. But for Chinese even the smallest and most remote details make an entirety and these are essential parts for them to close a deal. To negotiate with Chinese, you need to make time. Have patience. They appreciate it when you gradually build up your argumentation, avoid going all to direct to your main goal and take the relationship with your business partner in consideration (Li, Xiangling, 2009).

1.1 Investment vehicles

How do startups want to enter the (Chinese) market and as what kind of investment vehicle? Choosing the right Chinese business structure can be a confusing step for entrepreneurs, the therefore often seek contact with extern experts or consultants. Doubts like working with a company from a holding in Hong Kong, the need of a business partner or being able to do it all their selves often occur. On top of that experts give different advice. Some would say it is better to stick with local partners, others think that you should keep control yourself at all times. The kind of corporate structure and the type of holding you register depends on many different factors, such as: the market in which you operate, the operations that you want to perform in China, the strategic choices that you want to make and the possibilities that you have.

It all begins at choosing the market where you want to operate. The Chinese government roughly pointed out four different types of industries: normal, stimulated, prohibited and limited. When your company is part of the first two (normal or stimulated), you will have unlimited choice of the type of enterprise. When operating in the forbidden industry, you can forget China. Companies that are active in the limited industry are often obliged to work with a local partner. In this case, choosing a Joint Venture as company vehicle is the only option. A logical next strategic step to take in starting a company in China, has to do with what you actually want to do in this country. In this case there are three vehicles that are used: Wholly Foreign Owned Enterprise (WFOE), Joint Venture (JV) or Representative Office (RO).



Wholly Foreign Owned Enterprise (WFOE) is

by far the most common investment vehicle for mainland China-based business wherein foreign parties (individuals or corporate entities) can incorporate a foreign-owned limited liability company. The biggest difference that separated WFOE from other investment vehicles is the high level of managerial control: involvement of a

mainland Chinese investor is not required. Figure 4 – Investment Vehicle, 2012; Source Getty Images

The advantages of a WFOE are the just named level of managerial control, the ability to employ own people without restrictions, greater flexibility, possibility to convert RMB profits into US dollars and a greater level of protection of intellectual property rights (IPR). Some of the disadvantages of a WFOE are that the initial set-up costs are high and the incubation period can be quite long. As they choose to be more independent with this type of investment they have no access to Joint Venture partner resources with even higher start-up and operation costs (registered capital). Depending of the industry the company will invest in, there can be some limitations and there is a minimum number of staff requirement also according to these. On top of that the tax a repatriation of profits are severely challenging.

Wholly Foreign owned companies in China are limited liability companies (LLC), which are completely owned by one or more foreign investors. They are originally created to encourage foreign-run manufacturing and exporting activities. Since China's entry into the World Trade Organization (WTO) in 2001, limitations on WFOE's have been reduced to allow for their use in the service industry: the so called Consulting WFOE's. Many Western legal concepts are applied differently In China. For example, a company's different branches are not recognized in a WFOE because Chinese law does not have a clear definition of the term 'branch'. Therefore, any operation setup outside of the WFOE, such as a branch office or Representative Office (RO), is not part of the WFOE according to the Chinese law. The WFOE's registered capital must be solely by foreign investors. The ability to retain control of the enterprise makes WFOE in China by far the most attractive option for the majority of the investors.

You can divide WFOE's in China in three different types: Standard or Consulting, Trading and Manufacturing. *Standard or Consulting WFOE's in China* are licensed to conduct business in the consulting and service industries. *Trading* WFOE's are licensed to conduct trading, wholesale, retail and franchising activity, also referred to as FICE (Foreign Invested Commercial Enterprise).

Manufacturing WFOE's are the only WFOE allowing foreigners to conduct manufacturing activities. The set-up is the same as a Consulting WFOE, but includes an additional license for manufacturing.

In contrast to a representative office (RO), which is restricted to non-commercial activities, a WFOE in China is allowed to conduct business activities, including issuing invoices to customers and receiving payments in Chinese Yuan. And unlike with a Joint Venture (JV), WFOE's in China have no compulsory requirement to involve a Chinese partner and are free to implement their parent company's or their own strategies. They also have protection of intellectual property and property technology. They are licensed to import and export goods and have full control of human resources.

An important consideration when setting up a WFOE in China are the Article of Association (AoA), these articles form the operation rules of the WFOE in China, meaning shareholders are legally bound to operate according to the Articles they choose to establish. If the WFOE's Articles of Association are not prepared carefully, it can create significant legal problems for a company. For example, if a WFOE's Board of Directors Article is not designed with care, shareholders completely lose control of their company. Some of the important areas defined in the Articles of Association include;

- Scope of Business Article
- Production Scale Article
- Total Investment Article
- Board of Directors Article
- General Manager Article
- Profits Repatriation Article

The Business Scope is an Article that includes a one-sentence description of the industry and market in which the WFOE is planning to do business,

Chinese regulations stipulate that "foreign investors are permitted to set-up a 100% foreign-owned enterprise in industries that are conducive to the development of China's economic benefits, and not prohibited or restricted by China's government." This means a foreign-owned enterprise is only allowed to conduct business in certain types of industries and fields as defined in its business scope. It may seem tempting to define a wide Business Scope, but this is unwise because it can lead to post-licensing problems with the Chinese tax bureau. Adjusting the Business Scope requires new Applications and approvals which could harm a WFOE in times where flexibility is needed. It is the best to select an honest and clear Business Scope that both reflects their company's planned business activities and protects their ability to expand in the future.

Joint Venture (JV) is a business arrangement in which the participants create a new business entity or official contractual relationship and share investment and operation

expenses, management responsibilities, and profits and losses. The Chinese authorities encourage foreign investors to use this form of company in order to obtain exposure to advanced technology and new management skills. In return, foreign investors can enjoy low labor costs and a potentially large Chinese market share. Joint Ventures are sometimes the only way to register in China if a certain business activity is still controlled by the government. For example: restaurants and bars, building and construction work, car production, cosmetics etc.

There are 2 types of Joint Venture:

1. **Equity Joint Venture (EJV)**, this is, after WFOE, the second most common manner in which foreign companies enter the China market and the preferred manner for cooperation where the Chinese government and Chinese businesses are concerned. Joint Ventures are usually established to exploit the market knowledge, preferential market treatment, and manufacturing capability of the Chinese side along with the technology, manufacturing know-how, and marketing experience of the foreign partner.
2. **Cooperative Joint Venture (CJV)**, also known as Sino-Foreign Cooperative Venture, the parties involved may operate as separate legal entities and bear liabilities independently rather than as a single entity. A cooperative venture may also be registered as a limited liability entity resembling an equity joint venture in operation, structure, and status as a Chinese legal entity.

Advantages of choosing a Joint Venture (JV) is the opportunity to utilize existing sales networks and customer base as well as having access to partner's existing resources and production facilities. This all will also get you a lower cost base (local management). Although, there are also quite some disadvantages. Mainly the little managerial control and the fact that finding a trustworthy partner will be a critical asset. With a Joint Venture it is challenging to agree on the terms of the partnership because the partner will most probably negotiate terms in their favor, making the negotiation period very

likely a long one. WFOE and JV are very comparable as both registration procedures take about the same amount of time. For the registration progress of both vehicles you have to count at least 3 to 6 months. The big difference between the two is the ownership: a WFOE is completely in hands of a non-Chinese and a JV you establish together with a local Chinese party. The advantages and disadvantages of both structures, therefore, depend on if you want to work with a local partner or not.

Setting up a **Representative office (RO)** can be an effective way for foreign investors to get a feel for the Chinese market while demonstrating commitment to the market. Other than a distributor or agent that may have limited allegiance or little interest in end-user satisfaction. Some of the advantages of a RO are that it is the most accessible type of foreign investment structure to set up and, unlike the WFOE, has no registered capital requirements. The set up costs are low and especially for marketing, partner auditing and admin purposes this investment vehicle is an obvious choice. However, RO's also come with disadvantages, such as: the incapability for the company to trade, the limitation on the number of staff and the fact that the staff has to be employed via a third party (human resources agency) that will sign a contract with the RO on the one and with the Chinese staff on the other in order to ensure social security and housing fund. When you intend to get paid or pay from a Chinese organization, a RO is not the best option. This is only a structure to hire people. Also, the Chinese government is very strict in the approval of RO's due to past abuse. Many Western companies have used this construction in the past to arrange a visa for themselves.

The **Hong Kong Limited (HK Ltd.)** is another variant. This kind of enterprise on its own is useless in mainland China. The utility in an HK Ltd. lies in the ease. It is a lot easier to establish an entity in China when you do it out of a Hong Kong Limited structured Company. This structure will not be used by the startup companies that I am intending to contact for this investigation but did not want to leave it unmentioned as it is a structure that has been used in the past by foreign companies. This because it does have some advantages. When your organization would hang directly under a Portuguese holding, a lot of documents will have to

be legalized at the notary in Portugal and send to China. Through a Hong Kong Limited this is not necessary due to the conventions between Hong Kong and China. Next to this, a holding in Hong Kong can be beneficial for taxes.

A last consideration you would have to make is the type of adventure you want to make in China. What kind of possibilities do you have? Do you have the money, time and energy to focus on establishing a new company? Having a holding in China will take a lot of your time and money. If you don't have one of these, then it might be better to refrain from a Chinese company structure. Instead, a distributor or agent would possibly be way more effective. This means that you have to register, don't have to contribute capital and don't have to manage an organization.

Then there are also **Chinese Unicorns**. 'Unicorns' are startup companies that have not been listed yet, with a value above 1 billion dollars. The most famous unicorn in the world is Uber. The most known Chinese Unicorn is Xiaomi. These both at the same time are also the two most valued unicorns of the world. Startups like these have through their market share, market potential, possible unique technology and not in the last place their financial participants, a dominant position in their sector. They can (and have to) fetch more investments every time to stay ahead of their concurrent. "Go big, or Go home" is a statement that explains this quite well.

As seen in the figure below, next to the VS it is mainly China that masters this game quite well. From the top 20 unicorns 6 of them are Chinese (five as we don't also count Uber China) and only one from Europe. At this point (April, 2017) Portugal has three technological start-ups with a high potential to become unicorns in a short time frame, according to the classification of Tech Tour Growth 2017. Which means that they will reach a valorization of a billion dollar. Amongst these are: Feedzai, Talkdesk and Uniplaces. Aside of having an exceptional business growth, these pre-unicorns all have in common that they are 'machines' in creating posts of qualified work. Only these three startups already have created 335 jobs before the end of the year.

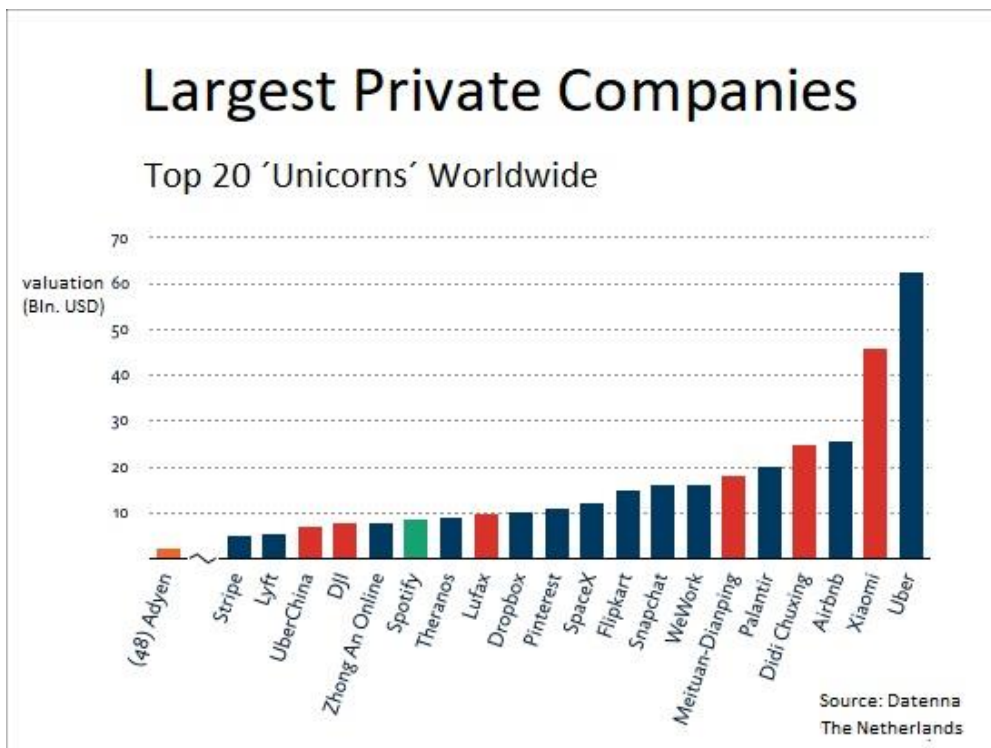


Figure 5 – Top 20 Unicorn Companies Worldwide, 2016; Source Datenna NL

A majority of the Chinese companies above have only been founded recently and most of them originate from mergers (fusions). Two of the Chinese concurrents of Uber, Didi Dache and Kauidi Dache, continued together last year with a value of over 16 billion USD. They are operating in more than 400 cities and own 87 per cent of the private car reservations. In October last year, the company changed their name to Didi Chuxing. Apple will invest 1 billion USD in this company, against a value of 26 billion USD.

Chinese startup companies and their investors manage to create enough market in their own country and in case of Xiaomi and DJI (a Drone manufacturer) also outside of that. If the problem for the seemingly substandard success in Europe is the fault of the lack of guts with European VC, we leave in the middle for now, the possible lack of a real intern European market of the expertise of European startups. Though it looks like that the last one is less likely, seeing that there are more European entrepreneurs in Silicon Valley do succeed.

1.2 Chances in China

Since European entrepreneurs have a shot in the US, the question rises if this is also the case in China. The starting of a company in China is easier than from example 5 years ago. But the Chinese language and especially the market is quite challenging. Venture Capitals are aware of this and therefore are more hesitant with delivering investments. Also the Chinese internet can lead to a lot of frustrations.

More and more you can see *incubators* and shared office spaces where foreign startups make a 'soft landing' in China. These facilities were also present a few years ago, but in that time the landlords only cared about the amount of square meters rented out. Nowadays people also advert more and more with juridical advices, pitch events, Wi-Fi and coffee. With the coming of the foreign 'co-working spaces' companies such as WeWork, is a positive sign that these kind of service providers trust their potential group of clients. Also from Portugal and Europe people are busy to improve the steps that startups have to take to get towards China.

1.3 Know your Chinese business partner.

However, when choosing to have a holding in China, whichever market entry mode is chosen, thorough market research should precede any final decision on how and when to enter the market. A growing number of market research companies now have operations in China, and the market is becoming easier to research than ever before. This also because of the outpouring of English-language publications on China available through the internet makes it relatively easy for Western companies to carry out some initial research on the Chinese market (Hedley, Mark, 2016).

With all the information given and the knowledge we have about China, Chinese history, culture and language, what would be the first important steps in negotiating with China? How to establish the first contact as a Western Startup company and how to negotiate with other Chinese companies. What are the difficulties and approaches with the Chinese language and culture? And most importantly: how is it possible to help or facilitate these young companies, as a Sinologist, in negotiating with their counterparts?

A logical and important first step is to get to know the people that you are doing business with. Who is this Chinese entrepreneur and how does he work? A lot has been written about this matter, concluding that a Chinese entrepreneur is like a bowl full of contradicts. The best description I could find is that from Annette Nijs, she claims that a Chinese entrepreneur is a combination of an ambitious pragmatic, a loyal bureaucrat, a Confucian gentleman and a warrior:

1. The Ambitious Pragmatic

The ambitions of Chinese entrepreneurs are high. Their common argument is: China has a lot of entrepreneurs, so there will always be a few that make it and grow out to be a top businessman. And why could that not be one of them? This combined with the approach of many Chinese that follow their instincts and observations and not that much a carefully chosen strategy, then you meet the Chinese Ambitious Pragmatic, somewhat opportunistic of character. The Chinese have their own version of the proverb “murky waters make good fishing” (one can benefit of the problems of others). Times change and insecurities give a wide range of business opportunities. After all, fish in clear water has been caught and eaten by others. The focused attitude and the “to go for it” mind set, makes the Chinese entrepreneurs very driven businessmen.

The Chinese entrepreneur is much focused on making the most out of chances and less on writing a balanced business plan. The focus of the Chinese is rather a short term than a long term one. The phases of generating and testing new products is often merged to win time. Chinese like to experiment and value more the trying out of a product at the consumer market to, as a result, gain experience, than let an extended market do research before. They focus less on existing opinions and market paradigms and try out more. “Let’s try”, is the typical attitude of the Chinese entrepreneur. When a new product fails on the market, a Chinese will accept this without a murmur and will try something else afterwards. Most of the times, he or she will have a backup plan ready that can start right away. The short term focus of the Chinese entrepreneurs has

everything to do with the here before mentioned fact that they deal with risks a lot easier than the Westerns.

2. Loyal Bureaucrat

Next to making their own money, Chinese also want to contribute to the future of their country. That comes as very natural for them. Collective of individual success give reasons for double pride: for your country and for you. Chinese entrepreneurs often take over the plans and objectives of their local government and of Beijing as a guideline for their own business. To respond to this the right way, success for the company can also mean success for the government, which in China is very important.

3. Confucian Gentleman

Chinese treat their business relations and clients with a lot of respect and often give them a very warm welcome. They like to use words of respect and trust, stress the importance of a relation with mutual benefits, ask about the well-being of your family and address you with “my friend”. There will not be negotiated but there will be conversation and extended dining. This way, Chinese express their interest in collaboration and partnership: nothing more and nothing less.

4. Warrior

When you look in to the heart of a Chinese entrepreneur, you can see the traditional warrior: he wants to win and can only accomplish this by defeating the others. The Chinese entrepreneurs strongly play the so called zero-sum game², when one player wins the other players have to lose as much. There is only one price to divide. He does this in a hidden way without giving the impression that he is on a warrior's path, preferably without walking away from the negotiation table. This way, the Chinese express that they are willing to compete. We do speak about a price war between companies. The Chinese think that the word “war” is overdone. They see these types of techniques as perfectly normal and admissible. They are masters in the warrior ship of Sun Zi (Huimin 544 – (?) c.a. 496).

² All or nothing

1.4 The importance of Guanxi

After discussing the different types of company structures and the questions whether which one to choose. It is very important to know on how to approach the Chinese market and other business partners. When dealing with Chinese there are, as in every different country culture, some ways and methods that have an origin in the history and culture of these people. Glued stuck in their way of negotiating, making and maintaining (business) relationships and view on us foreigners. A common knowledge in China, her history and culture is recommended, but it all starts and comes back at one important red wire that goes through all aspects: Guanxi (关系), the Chinese word for relationship. In China they are convinced that relations are more important than laws.

Guanxi is for networking, but then the Chinese way. Networking, the Chinese way, is very important in China. In comparison with other European countries, the Chinese society is focused rather on a group than the individuals. Collectivity had a much wider meaning than with us Europeans and that does not even relate that much to their communist history but more with their tradition going further back in history. This tradition is called Guanxi. Confucius (Chinese philosopher, 551 BC – 479 BC) already pointed out the importance of relationships and that people are defined by these relationships. Guanxi puts means in the connection that more people that share a group identity have. The highest bands are of course those between relatives, but also between people that have lived in the same neighborhood, went to the same school, worked at the same company or have the same religion, can become a network based on Guanxi. Roughly said, Guanxi simply is a personal relation between people. The concept can also imply on the whole network that someone can rely upon and mostly it stands for an understanding and respectful relationship between people. You do not really have to know each other with Guanxi, when person A and person B both know person C they already make part of the same Guanxi.

The whole idea behind Guanxi is that you make the relationship with one person as a priority rather than the value of the transaction. When you do that, it automatically means that you want to keep to a certain promise or agreement, or that you want to do something

for someone that did you a favor in return. Because when you do not, there is a big chance that you put this relation at risk, and through this person, other relations as well. That is a high price you would have to pay. Guanxi has influence on how people treat one another. It motivates to keep you to your agreements, keep your promises and do something in return.

The Western way of networking focusses more on the relation between organizations, while the importance of Guanxi is to establish and develop personal relations. Recent western management techniques like in the book *The Speed of Trust* from *Stephen M. R. Covey* are quite useless for the Chinese because these types of cases are already in their genes. They, netter than anyone else, understand that a personal bond, marked by mutual trust and respect, through understanding and personal involvement, can be crucial parts in business relationships.

Guanxi is not only very closely linked in practically every aspect of the social life in China, also companies use Guanxi as a strategy to be competitive. Guanxi is mainly beneficial for companies that do not have strong ties with the Chinese government. From an investigation of Xin and Pearce it seems indeed that managers in private Chinese companies give more value to Guanxi and use it more than colleagues in state companies.

There are several ways to 'use' Guanxi. For example through the development of a new market in an area where the company has no establishments yet, Guanxi helps to make the first steps. Guanxi can also help as a social safety net for companies. Imagine if you are as a company money wise and you temporarily cannot pay your distributors. In the West you would have to go to a bank and hope that they would lend you the money to pay your suppliers. In China it is a lot easier to delay the payment because a lot of these suppliers make part of your Guanxi network. They accept a delay of payment, simply because you also would do the same for them when needed.

A special advantage of Guanxi above Western ways of relation management or networking is that there arise all different kinds of co-operation ties and allies, with all kinds of extra ordinary results. Western companies search their network as mentioned earlier, mainly inside their core business, while Chinese step out of that with more ease because they

use Guanxi relations with companies of a completely other branch of business. This is also one of the reasons that many companies are so called conglomerates with many different products and services.

The Guanxi between companies often takes over the part of complicated contracts between companies about services that one company has to deliver to the other. According to Lee Kuan Yew, founder of the Republic Singapore, the Chinese use Guanxi to compensate the lack of law enforcement and transparency in the law and order regulations.

Through the tradition of Guanxi a lot of Chinese companies are further than Western companies in the way they use the relations of their employees for the benefits of the company. The so called social or relational capital of Chinese companies, therefore, is bigger than those of Western companies. Chinese have gained the art of building trust and therefore the idea of the before mentioned book “The Speed of Trust” of Stephen Covey, together with their traditions.

Western managers and entrepreneurs are clever to very aware reinforce their own network by not only commercial but also social terms of thinking of co-operation with organizations outside the company. Besides that, Western companies are smart to try to become an insider of Chinese companies.

Guanxi, according to Jochum Haakma (Former consul-general in Hong Kong, Shanghai), is a network chain of relationships and knowing who the right people are that make the important and final decisions. You will always need a Chinese that has a good Guanxi in the region and sector where your company operates. Entrepreneurship Chinese Style – everyone that speaks to people that do business with China, gets to hear about their joyful dinners, with or without loads of Baijiu (白酒, rice wine) and karaoke, and the tough negotiations about contracts. There are also stories of Chinese that do not hedge back to fiercely negotiate with a foreign partner.

1.5 The 36 Stratagems of Sun Zi

During the classes Management and Negotiation, given by Dr. Professor Nelson António, we got lessons thought out of the book of Dr. Professor Virgínia Trigo: “How to Negotiate in China” (“Como Negociar na China”), on how to negotiate in China using the 36 Strategies inspired on a book that was discovered in 1941, in Sichuan province in China. It was a reprint of an earlier book of the late Qing or Ming dynasty. The only extend copy of a book that had existed for nearly 2000 years: The Secret Art of War, the 36 Strategies. Who has wrote the book nobody truly knows. Some legends claim that the hero of the three kingdoms era Zu Guoliang was the original author when yet other legends claim it was the work of the famous strategist Sun Zi, author of The Art of War. He convinced the emperor of Wu dynasty, stationed in the east part of China, that in order to win the war with the Chu’s that occupied a much bigger territory and had a larger army, they should follow these 36 strategies.

With no further information about the origins of the 36 strategies, current speculations suggest that there was not just one author but several ones. More likely they were simply a collection of idiomatic Chinese expressions taken from popular Chinese folklore, history and myths. It is believed that sometime in the early Ching dynasty some enterprising editor collected them into the form that is presented to us today. The original text of The Secret Art of War is quite short, only 138 Chinese characters. The book was divided in to 6 categories of 6 strategies each. Each strategy is in form of a Chinese proverb (成语) with a short explanation. Using 6 factors which contain each 6 strategies Sun Zi explained how it was possible to predict of both armies who would win the battle. The 36 strategies that Sun Zi wrote down in his book The Art of War are still used, not only for war but also in the commercial world. Many generals where inspired by Sun Zi’s strategies like Napoleon and many Nazi army leaders in the Second World War.

The 36 stratagems is a collection of 36 Chinese proverbs about unexpected actions, tricks, deceptions and strategies that can be applied in war, politics or the business world. I have tried to give my interpretation to the Chinese name of each stratagem and its explanation. Some stratagems have a story that related them to a historical event explaining their origin.

And then there is the way we apply the stratagems today the day on negotiating and doing business with China.

Group 1: stratagems to use in case of superiority. This group exist of more objective stratagems and, therefore, more easy to understand. In general, we assume that we are in a superior place when we have more means, more time and more people to fight or negotiate with.

1. Cross the sea in open camouflage 瞒天过海

The more continuous things and behaviors are, the less attention they attract. This stratagem revers to a part of the life of emperor Tang Gaozong of the Tang dynasty. *During a war against the Goguryeo (高句丽) the emperor refused to pass the ocean. On a day a general told him that he was invited to have dinner with a rich subject. Emperor Tag agreed and left with his entourage. When he entered the house of the subject he noticed that everything started shaking. He was lured on to a ship. With the discovery of this betrayal the emperor still decided to continue the journey and won the battlefield.*

The general in this case cheated the emperor to cover up his goal. The emperor didn't see any harm entering a house, and why should he? That is something we do every day. By not revealing his plans the general was able to reach his goal.

Translating this in to business language it means that you reach less if you try to impress with a flood of ideas and prepositions. Some well-placed actions often have more dramatic effect and a bigger chance of succeeding. If you try to stay unnoticed, don't do anything extreme.

2. Surround the Wei kingdom to save the kingdom of Zhao 围魏救赵

The thought behind this stratagem is that when you are dealing with a stronger enemy you should avoid man to man confrontations. Instead, you should search for a weaker spot that you could use indirectly to attack the enemy.

This stratagem comes from the period of the Warring States. The state of Wei attacked Zhao with which they tried to conquer the capital. Zhao asked the state of Qi for help, but the general of Qi, Sun Bin, realized that it would be a bad idea to fight from man to man with the army of Wei. Instead of that he attacked the capital of the Wei state, Daliang. The army of Wei, which was exhausted of battling in the Zhao state, hurried its way back to defend their capital. However, they were ambushed at the battle of Guilin.

While doing business try not to 'fight' with the bigger companies but try to look for a niche market³ in which you can develop.

3. Commit murder with a borrowed knife 借刀杀人

The meaning of this stratagem is to let others do the dirty job.

In the time of the Three Kingdoms: Wei, Shu & Wu. Guan Yu, a general from the Shu kingdom, was in fighting Cao Cao in the battle of Fengcheng. Cao Cao sent an advisor to Sun Quan from the Wu Kingdom to encourage him to attack the Jing province and gain its ground. If he would succeed, all the land south from the Yangtze River would be given to Sun Quan as a reward. Within a few weeks Sun Quan attacked the army from Guan Yu in Jiangling where he was forced to pull back. Guan Yu was captured and executed.

In companies this means to use somebody else's skills to gain for yourself. For example: using borrowed money to monopolize companies.

4. Wait patiently for an exhausted enemy 以逸待劳

Choosing time and place for a battle can be highly in your advantage. This way you know where and when the battle will take place while your enemy wastes time on

³ a smaller part of a market that knows less concurrence than the main market

useless quests. The extra advantage you have is that your troops are well prepared for the battle and can spare their strength while the enemy has to work to reach you.

In the battle of Maling, the troops of Wei where in the majority compared to those of Qi. The general of the Qi troops ordered them to pull back. The Wei troops started following them and the Qi where capable to prepare an ambush in which the exhausted Wei soldiers where an easy victim.

In the commercial world the highest risks are often made by the smallest companies. It is known that big companies often use smaller companies to explore speculative innovations to avoid expenses and risks themselves. Only at the moment that the plan turns out to be achievable the big companies take part.

5. Plunder a burning house 趁火打劫

During war it is preferably to attack the enemy when he is at his weakest. Especially when the attack is from the inside the enemy will have little time to deal with the threat. *A long war between the warriors of Han and Chu finished in a pacification. While the soldiers of Chu pulled back from Han grounds, Han Xin and Zhang Liang advised the general of Han Liu Bang to attack the Chu. They also told that in the Chu Kingdom there where a lot of governors that where very interested in the position of Liu Bang. They said that the willingly escape from the general of Chu Xiang Yu would be the same as “setting free a tiger so that it could come back later to kill his owner”. After some consideration Liu Bang decided to attack Yiang Yu and this meant the end for the Chu Kingdom.*

Commercially seen it is preferably for companies to specialize to find undervalued or poorly managed companies. Which is seen a lot in the financial sector concerning investment banks and financial workers.

6. Make noise in the east and attack in the west 声东击西

Somebody that is capable of the element of surprise is in the advantage. One of the ways to use the surprise element is to let your enemy think that you are preparing for an attack from a certain point while actually the true attack is headed to another vulnerable place.

This stratagem is one of the many that is adopted by Sun Zi in his book The Art of War. Let your enemy use his recourses and distract him from your actual goals.

Credit card companies are experts in applying this strategy. They attract people with low monthly costs while they hide the high financial costs that can appear with the usage of the card.

Group 2: stratagems for defense. This group of stratagems is used when you are being under attack or being in confrontation with another party.

7. Create something out of nothing 无中生有

The simplest interpretation for this strategy is lying. You can make your opponents believe something that is not there, is there. Or make them believe something that is there, is not there.

In an incident during the battle of Yongqiu and Suiyang, the soldiers that where under fire came up with a plan when they found out that they had used up all of their arrows. General Zhang Xun gave the order to his men to make thousands of scarecrows. One night the soldiers dressed the scarecrows with their uniforms and made sure that the enemy could see them from a distance. The Yan army shoot on the scarecrows and the Tang therefore was able to collect their munition before the Yan found out they were not shooting at the actual soldiers of Tang. The next time that they thought they saw the Tang soldiers, they didn't even take the effort to fire one arrow. But this turned out to be a mistake because this time it where the actual soldiers who could easily attack Yan this way. As a result the army of Yan had to pull back.

A positive interpretation of this is innovation. In the commercial world innovators are people that see how they could become and not only who they are now. They are the

pioneers in developing production and services of which others have not even thought about yet. Like Google for example.

8. Mend openly the mountain roads, but sneak through the Chencang passage 暗渡陈仓

This stratagem explains that you can distract the opponent with something from what you are actually doing.

Liu Bang pulled back to Sichuan Province to prepare his army for the confrontation with Xiang Yu during the Chu-Han battle. When he prepared his troops he sent some of his soldiers to repair the mountain roads that he had destroyed in a previous battle. When actually he was leading his army secretly through Chancang to Guanzhong. Xiang Yu was so distracted by the Liu Bang's troops that were fixing the road, which would take them several years, that he didn't consider him a threat anymore. This given, Liu Bang had all the time to plan a surprise attack which led to the fall of Xiang Yu and the birth of the Han Dynasty.

In the business industry you can pull the attention by following a particular route while developing another plan at the same time.

9. Observe how fire burns at the other side of the river 隔岸观火

Another saying in Chinese for the same idea is: "Sit on the mountain top and observe how the tigers fight".

Newcomers in the business industry have to be conscious of opportunities when big companies are in battle with one another. When a large company decides to compete against another large company, the smaller companies often have a chance to respond to this and to take over a part of the market.

10. Hide your knife behind a smile 笑里藏刀

The meaning of his strategy is not a difficult one. First you have to win the trust of your component and the moment he stops seeing you as a threat, you attack. It is not a kind way, but a simple one.

Business related this stratagem also has a positive side: it suggests that sometimes it is needed to present a negative situation in a positive way just to turn it in to something more pleasant.

11. Sacrifice the plum tree to save the tree with peaches 李代桃僵

We in the west have our own version of this stratagem: “lose a battle to win the war”. *During the period of the Three Kingdoms, Cao Cao used this stratagem. During the siege his stock was running low and he instructed his commander to use more water than rice to save up the grain that was still left. When his soldiers started complaining Cao Cao gave the orders to execute the commander while telling his troops that the commander sold their rice stocks to the enemy. Therefore the attention of the soldiers was not projected on the lack of food and as a result their moral increased and they were motivated to win the battle fast.*

When doing business it is often tempting to focus on short term goals. Forward looking and successful businessmen often don't hesitate choosing to ignore the short term profit that does not benefit the long term goals. Applying these strategies takes courage and determination, especially when sometimes there have to be made offers.

12. Seize the moment to scrounge a goat 顺手牵羊

A stratagem that does not need a long explanation. Men that are on their way to battle need to be open for the little opportunities that come along their way, such as a residual goat. The moral is that no chance is too little, this also counts in doing business.

Group 3: stratagems for attack. This group of stratagems is used favorably in cases where the initiative is yours.

13. Beat on the grass to scare the snake 打草惊蛇

Do something that is surprising for another. It might frighten the enemy. Watch what the reaction of the other is and take advantage of signs of confusion or fear or any mistake that might occur. It might give you useful information while you prepare for the main battle.

During the Tang dynasty, the bookkeeper of a not so loved bencher named Wang Lu received a letter from the local people accusing him of corruption. Wang Lu wrote on the letter 'by merely beating the grass, you have startled the snake hiding within'. This perhaps implied that he recognized the trick, and was ready to fight back. He also realized that the stratagem had worked well as a warning to him that the population would not allow his corrupt ways of ruling.

An opponent that is not moving can be confusing as their strategy seems unclear. A common tactic in martial arts is to stamp or slap to provoke a reaction, making them move in the direction they were thinking about. Sending letters from lawyers is a common way of startling both individuals and companies. This can be used to make them back down from outrageous claims.

14. Borrow a dead body to wake up the ghost 借尸还魂

Take something from the past and re-use it in some way. This can include using variations on old ideas, bringing them up to date, adapting them to modern use or fitting them into a broader strategy. In business, plans and strategies which were shelved in the past may now be applicable. *The Empress Lu adopted a series of boys as her own in order that they may 'succeed' her dead husband and so keep her in power. Puppet rulers have been used throughout history, where the nominal king or emperor is actually under the control of powerful generals or business people.*

The general principle of reuse is to find what works and ensure the knowledge and learning from this is continued rather than being rejected as 'old stuff'.

15. Lure the tiger to come out of the mountain 调虎离山

this stratagem explains that to face your component is it easier to lure him away from his high or comfortable position and force him to face each other on fair ground, if not your ground. *Gen Yang wanted to defeat the powerful Fei brothers, so he besieged Fei Gan while also lying in wait for Fei Yi, who was killed as he came to his brother's rescue. Gen Yang then paraded Fei Yi's head on a pole, leading to Fei Gan and his people fleeing.*

When negotiating, the game of diplomacy can be played smart with an advantage of the people that are on their own territory.

16. Let something go first to catch it later 欲擒故纵

When the enemy is fleeing, chase them for a while for a while in order to exhaust them before you attack or capture them. If they are unable to escape, use shows of strength and other methods to demoralize them and sap their willpower. Allowing the enemy to leave can also be a good strategy when you plan to engage them in more advantageous situation.

In business you can allow competitors to spend a lot of money before taking them on in product development or marketing. Internally, instead of punishing a person you can let them know they deserve it but you are giving them a chance.

17. Throw a brick to catch Jade 抛砖引玉

Offer somebody something small in order to get something big. Present them something of what seems to be of worth to attract real worth.

This stratagem comes from the time of the Tang dynasty, the poet Chang Jian wanted to learn from the great poet, Zhao Gu. He wrote half a poem on a temple wall where Zhao was visiting, hoping the better poet would complete it, which Zhao did.

When doing business it is common to use rewards such as bonuses to effectively lure people in working harder in achieving the goals of the company. Frequently used in China with national or international negotiations.

18. Defeat the enemy by taking its leader 擒賊擒王

When the enemy has a mercenary army, attack the leader. His death will often lead to the falling apart of the army. A variant on this strategy is to capture or destroy anything that they hold dear or which is a motivating force for the opponent. Applying this stratagem when negotiating is a little less aggressive: when we want certain decisions being made, it is best to go talk directly to the boss instead of trying to talk to several employees.

Group 4: stratagems for confused situations. The following stratagems are mainly used in situations that are unclear or uncommon.

19. Secretively take away the firewood from under the kettle 釜底抽薪

Being creative and looking for ways to take the strength of the enemy to weaken their purpose. Any resource or thing they use can be attacked, including psychological resources.

In the time of the Three Kingdoms: Wei, Shu & Wu, Cao Cao was sieged by Yuan Shao. Therefore he used a part of his soldiers dressed in the enemy's clothing to infiltrate the enemy camp and set fire to their grain stores. This not only caused them problems but created immediate fear. As a result Yuan Shao's troops were terrified and confused and all over the place.

Many refer to doing business in China as a fight. Mostly because we like to keep on to the timescale with the time we have scheduled for being there. From getting out

of the plain until getting in it again, everything is scheduled strictly: hotel, transport and meetings. Chinese are aware of this and this gives them an advantage in the negotiation.

20. Roil the water to catch the fish 混水摸鱼

Take advantage of confusion and chaos. *After Cao Cao was defeated, Liu Bei established the kingdom of Shu taking the strategic Yangtze city of Jinzhou. He then took Yizhou while internal struggles distracted the dominant forces there.*

One of the most important factors that let you take advantage of chaos is readiness. In case of negotiating it is important that you plan ahead, seeing possibilities and then staying alert to catch the weak beginnings of chaos.

21. The cicada sheds off its golden skin 金蝉脱壳

Act as if you are doing one thing while doing another, for example: Appear to be doing nothing when you are actually taking serious action.

In history Country leaders have often used body doubles to make it appear they are in one place when they are elsewhere. This has been used when the leader is sick, elderly or is afraid of being assassinated.

Negotiating, especially in China, does not only takes place in the meeting room. It will involve dinners, banquets and even karaoke gatherings to make the business deal complete.

22. Lock the doors to catch the thief 关门捉贼

Tempt your enemy into situations where their own actions will only cause them further trouble.

When Bai Qi was fighting Zhao Kuo, he first let Zhao win a battle and then challenged him to a final match in a position further toward Qi. Bai Qi let his enemy win again

while quietly cutting off their supply lines. Starving, Zhao's forces began killing one another for food. In a desperate attempt to break the blockage, Zhao was killed and his army surrendered soon after that.

If you really want to take over your component then don't pity him while he is in his disadvantage. Some foreign companies with enough authority in the negotiation process, choose to invite the Chinese company to another big city. They pay for Hotel and transport just to be able to make a negotiation on 'ground zero' with them.

23. Befriend a remote state while you attack a neighbor 远交近攻

Do not make war in remote places while you ignore the ones that are closer. Rather, make alliances with those further away in order to conquer your neighbors. While negotiation it can be an effective strategy to make alliances with companies which are closer to your company in using their facilities with logistics for example or even to force the remote companies to negotiate on multiple fronts.

24. Pretend as if you just want to use the Guo state as a passage and occupy it 假途代虢

When two of your enemies are in conflict with one another, intervene on behalf of one of them. This stratagem works best when the borrower is more powerful. Companies and people like to keep powerful others friendly and so will tend to allow more. Powerful people, however, may not be that trustworthy and may take advantage of a smaller ally knowing that the party cannot take revenge for a betrayal.

Group 5: stratagems for gaining ground. This following group of stratagems is mainly used to obtain what is under the control of the opponent.

25. Replace the beams with rotten timber 偷梁换柱

Destroy or damage the sustaining structures on which the component depends. Seek to replace these with systems which you control. When you have rebuilt their house, they are under your control, quite possibly without knowing this.

Lu Buwei of Zhao impregnated a concubine and tricked Yi Ren, the prince of Qin, into marrying her and naming her first child as his heir. He then poisoned Yi Ren's father and the prince appointed him prime minister. Yi Ren then mysteriously died and Lu Buwei took over as the young boy's protector and even picked up again with the concubine. It is about trust. In order to replace pillars you need careful manipulation and long-term thinking. It often requires that you first get close to the other side or their allies or advisors.

26. Point at the Mulberry tree while cursing at the Locust 指桑骂槐

The metaphor of the name is that while you are doing one thing (pointing at the mulberry) you are really taking another quite different action (cursing the locust). Sun Tzu wanted to show the king of Hu that even women could be trained to be invincible. He created two regiments from court women and put the king's two most-liked concubines in charge of each. He then gave them marching orders, but the groups just giggled. He had the concubines beheaded and put two women from the front rows in charge and gave the order again. This time, they obeyed. In this way, Sun Tzu made his point to the king.

Distract yet the people that you are negotiating with by making them believe that the essence of the negotiation is someplace else than where it exactly is.

27. Play the fool without losing your balance 假痴不癫

Play foolish or weak so they do not take you seriously. Conceal your strengths until it is the best time to reveal them.

Liu Bei was plotting to overthrow Cao Cao. Cao Cao came to visit so Liu Bei pretended to be crazy in case Cao Cao knew about the plot. In this way he avoided detection. In business this is often used with eye on gender differences. Women are still seen as a less threatening component than men.

28. Lure somebody to the roof and take away the ladder 上屋抽梯

after an action is taken, ensure there is no going back. Isolating them can both motivate them to fight hard or alternatively demotivate them. Seek to create the motivation you desire, for example by cutting off enemy troops from their leaders and thereby confusing and de-motivating them.

'Management by Crisis' is often used in business to force action, where deliberate 'burning platforms' may be created and talked up.

29. Deck the tree with false blossoms 树上开花

Appear powerful even when you actually have far less power. Power is not just the real potential you have, it is also the assumptions of your power that others afford you. You can create illusions to help this and so create caution and fear where none is really needed.

In business, making the company and products appear more than they are is commonly used in marketing, where appearance can be more important than reality. Companies that appear larger than they are engender more trust. However, this may lead to competitors fighting harder against you, so intelligent caution may be needed.

30. Make the role of the host the one of the guest 反客为主

Treat your guests like hosts to be able to exploit their weaknesses. *Although Liu Bang conquered Qin, he let his stronger ally Xiang Lu take over as ruler. While Xiang Lu relaxed, Liu Bang built up his forces and eventually attacked and conquered Qin (Xiang Lu took his own life in shame).*

The business world is a constant changing scene of alliances and takeovers of various kinds. Moving into a new market a company may be a useful 'guest' but turn in to a 'host' as it achieves domination.

Group 6: in case of surrendering. This following group of stratagems is used mainly in cases where you are in a weak position.

31. Send your enemy beautiful women or objects that he will not be able to resist 美人计

Present your opponent with something that distracts his attention or takes his energy. *In 199 B.C. the emperor of Han, Gaozu, realized that he and his army didn't stand a chance against the invasion of Xiongnu. They pulled back in the city Pingcheng but soon were attacked by 300.000 soldiers of the enemy. When all hope of winning had flown, the advisor of the emperor thought of a plan. He sent a painting of a beautiful Chinese princess to the wife of the commander of Xiongnu, together with a note saying: 'My emperor's intention is to surrender to your husband and to have his mercy, he will send one of China's most beautiful women to be his concubine.' The wife of the commander became very jealous and ordered her husband to immediately stop the attack on the city and recoil. The next morning the Xiongnu army went home and Gaozu and his troops were safe to return back to their families.*

In meetings with foreign companies people often use young and attractive interpreters to take away the attention or soften the negotiation a little bit.

32. Open pair in pair the doors from a city off guard 空城计

This strategy is from 149 B.C. when Kong Ming and his army felt the need to pull back after a lost battle with the state Wei. With much less soldiers and without the capability to recoil they escaped to the city Yanping with the Wei army very close behind them. Kong Ming gave the orders to remove all flags and guards from the city walls and leave all ports wide opened. When the army of Wei approached the city, they only saw some men whipping the courtyard and Kong Ming playing a flute in one of the towers. Assuming this was a trap, the Wei army decided to turn around and leave.

Nowadays, this stratagem suggests that showing a weakness can be seen as a sign of confidence and strength. A superior will probably respect you more when you recognize your weaknesses instead of trying to hide them.

33. Try to create a divide between your enemies 反间计

Weaken your competition to create discordance between him and his allies. *In the late Wei Dynasty emperor Tai Wu and his army had General Zang Zhi and his troops located in the city Yu. Self-assured of the fact that his enemy would suffer*

hunger, he sent a chariot with a large bowl of wine in to the city with a message asking for a traditional wine exchange before the siege of the city. Zang Zhi used this opportunity by sending a pot with wine and a stamp of the wine maker back to Tai Wu. The wine, however, turned out to be urine which made the emperor furious and made him decide to attack the city in an instance. Zang Zhi and his troops were very well prepared for this and disarmed more than half of Tai Wu's army and win the battle.

In negotiation a lot of investors do not feel comfortable at all to talk about the subject matter of the meeting. They believe that the interpreters they have, were given to them with false intentions by their Chinese partners.

34. Wound yourself in order to win the empathy of your enemy 苦肉计

By acting if you are hurt your enemy can become overconfident and think that you are no longer a threat. This stratagem plays in to the sympathy that people in general feel for others that are less favored.

When times are hard for a company, the people in charge can somewhat liberate the suffering by, for example, making pay cuts.

35. Combine strategies 连环计

When you lack resources, then use all rules and strategies to try to be smarter than your enemy. By applying different methods it is possible to stay in control over the battle. When this is done successfully you will always have a back-up plan in case one strategy fails and your component will hopefully become his own enemy.

36. If everything fails; retreat 走为上计

When the situation seems hopeless, recoiling or regrouping seems the best option. You could also give yourself in or close a compromise. Pulling back does not mean defeat, you simply just put a step back so that, at a later moment, you can give in with full power.

2. Method

In order to find out the difficulties that Startup companies have when reaching out for the Chinese market, they need to be investigated better. With what product are they working and in which branch. Why do they think China is such an essential partner for them to do business with and if they have already any knowledge about the Chinese negotiation field and the Chinese market. Is it essential to also know about Chinese culture, history and language? And the other way around, what is important for these Startups, how does China gain their trust? Are there different kinds of strategies? And if so, which one works best for which branch?

To get answers to all these questions and to gain a clearer image of how to help these young entrepreneurs in their first steps to open up doors for their companies with China, they have been contacted. A selection of 10 Startups in Portugal has been made, established in 2004 to 2015, with as a goal to enter the Chinese market.

Contact with authorities like the Chinese Chamber of Commerce in Portugal, 1421 Consultancy Group and Chinaccelerator have been established, some of them were already contacts made while working for UHP. A list of Startup companies in Portugal has been consulted and contacted by telephone, email and, if necessary, by going there myself and introduce an enquiry with questions that have been found essential to know in the investigation to throughout the making of this thesis.

2.1 Help from within: consultancy groups, private and governmental

Jorge Torres Pereira, the Portuguese ambassador of China, gave an interview in the *Sábado* earlier this year, being congratulated for his award of Economic Diplomat of the year 2016 he answered some questions about the difficulties of young Portuguese companies that want to enter the Chinese market. The first question was if he considered it to be difficult for a Portuguese company to enter the Chinese market?

Jorge Torres Pereira answered: “The difficult part is, above all, finding the right partner. The market is not easy, there exist restrictions in relation to the different sectors that we can

invest in. There are cases that there always has to be an association with Chinese companies. There are various bureaucratic difficulties and an official governmental approval is needed of which the understanding is very important. One of the ways to pass some of this passivity is to express my worries about the fact that a company is having difficulties. Normally that is a way to overcome such a problem”. Did he feel like that these characteristics of the government facilitate or make it harder for a company? JTP: “The Chamber of Commerce complains about that there is an increase in difficulties, above all, in relation to the meeting of expectations. There was made a decision by the plenary of the Chinese Communist Party in the light of having more market and economic changes, almost like a paradigm change. This all assumes that foreign and Chinese companies had the possibility o compete equally. That is not happening. In some cases, instead of having more market, there is even less. There was a bet made in the “National Champions” that makes the competition with the European companies even more difficult” (Público, 2016).

To overcome these difficulties and to be really fully prepared when bringing your company to the Chinese market, it is important to seek help from within. A consultancy group can help you with this, but a lot of information and preparation an also be done with The Portuguese Chamber of Commerce. Please see below a small introduction of these assisting organs.

2.1.1. The Portuguese Chinese Chamber of Commerce

The Portuguese Chinese Chamber of Commerce (Câmara de Comercio e Industria Luso-Chinesa – CCILC) was founded in 1978. It is a non-profit private entity devoted to the development of the economic and commercial relation between Portugal and the People’s Republic of China.

CCILC’s governing bodies include the most relevant industrial and financial groups in the bilateral context, among almost 300 associated companies. Its head office is in Lisbon and it had a representative office in Macao.

The CCILC was founded before the re-establishment of the diplomatic relations between Portugal and the People's Republic of China. It was the first association of companies in Europe promoting business with China through the organization of missions, providing useful information and high technical support services, so that the associated companies could develop their activities in both countries in a more efficient, informed and safe way.

CCILC offers qualified technical support services, that allows its associates to develop their entrepreneurial activity in Portugal and China, in the most effective, safe and informed way.

Also allied is the Portugal – China Association of Young Entrepreneurs (Associação de Jovens Empresários Portugal-China – AJEPC). It was founded on the fourth of June 2012 and is, like the Chamber of Commerce, a nonprofit organization that was established out of the congregation of efforts from a group of Portuguese businessmen with as an interest to strengthen their position in the Chinese market, of which sharing the same vision, and same constructing spirit, they commit in the approximately, development and investment in both markets, Portugal and China, using Macao as a linking and strengthening platform in the economic and commercial cooperation between both countries.

Institutions such as the CCILC and AJEPC, are a bridge to young start-up companies that want to do business in China. The Chamber of Commerce even has a step to step plan built up to guide these young entrepreneurs during the first steps they take and help with the difficulties that may occur. (Câmara de Comercio e Industria Luso-Chinesa – CCILC, 2017)

2.1.2 1421 Consultancy Group

1421Consultancy Group was established 2005 by a Dutch founder named Peter Pronk. The company's main office is in Beijing and they also have representative offices in the United States and Amsterdam. Their main objective is to help foreign companies to enter the Chinese market. They do this by starting with defining the company's strategy, finding the right way for the company in question to enter the market and doing a necessary market research beforehand. They provide supporting service helping with all the documentation and

paperwork to legalize the company. When a company has been settled and functioning, 1421 often stays tied by helping it with administration and follow up plans. 1421 Consultancy helps with the following steps:

1. Business Consulting Services: researching your company's market, advising on entry strategy and helping to find partners.
2. Corporate Services: registration of WFOE, change the business scope and add and import or export your license.
3. Accounting Services: they make sure that the administration of your WFOE is done according to requirements and Chinese regulations.
4. Management Services: they help a company to manage their operations in China.
5. Optimization Services: They analyze your business, in order to help to optimize your organization.
6. HR Services: They help with all HR requests and issues.

During a conversation with Michael Pronk, son of Peter Pronk and International Business Development Director at the 1421 office in Amsterdam, he gave a bit more about the company and their services. But most importantly, their view on the importance of knowledge in Chinese culture and language when negotiating in China was broadly discussed. As both father and son, have not done a China related study but learned about China while being there, they emphasize the fact that you have to have a certain open mentality when entering the Chinese market. Most importantly: do not have expectations, expect the unexpected. Their company 1421, mainly assists in setting up a strategy and legal aspects of a WFOE or JV in China, but strongly recommends to, next to that, also consult bureau that helps to over bridge cultural differences and etiquettes. (From the interview with Michael Pronk, 2017)

3. The Investigation

For this investigation 10 Portuguese Startup companies that are established all after 2005 and have shown interest in entering the Chinese market, have been contacted. These Startups are

successful and are all co-founded by Portuguese entrepreneurs. The type of business and product is different for each company. In order to find out for each company what their ideas about China are, where they think their chances lie and what kind of help they are willing to take. Are they aware of the difficulties and obstacles they might come across?

All companies have filled in the same questionnaire and based on the answers given, to see how far these young startups have gotten already with getting informed about China and its way of negotiating. Questions such as: “How would you describe China in 3 words” and “have you thought of hiring a company that helps you with legal matters and can inform you about certain procedures?”, got the right answers to draw conclusions and maybe guide these companies into making sure they are well prepared before taking their company to China.

3.1 Questionnaire

- How would you describe China in 3 words?
- Have you made concrete plans about entering the Chinese market?
- Are you informed about the different types of investment vehicles (WFOE, JV & RO)?
- Why do you want to enter the Chinese market with your company? What does your company has to offer to the Chinese market?
- Have you heard reviews from colleague companies that have entered the Chinese market before yours?
- Have you thought of hiring a company that helps you with legal matters and can inform you about procedures?
- Are you familiar with the term *Guanxi*?

3.2 Portuguese Start-up Companies

Not all companies that were contacted, replied to right away. Therefore there had to be made contact to several companies more than once and others had to be left behind in order to make contact with new found companies. At last, a list from 10 companies, Portuguese

startups have filled in this thesis' questionnaire and therefore gave a better insight in where these companies stand with entering the Chinese market or not and how they think of China and complications they might come across. In the following chapters all companies have been introduced and described, that have participated and drew attention while writing this thesis focusing on innovative young companies from Portuguese origin that were thinking of, just about to or had recently already entered the Chinese market.

A List of participating companies. Following companies have had one responsible fill in this thesis' questionnaire and for the same purpose there has been contact with them or colleagues of them to hear their motivation to what and how they answered the questions about investing in China:

1. Aptoide
2. Farfetch
3. Feedzai
4. Findster
5. Science4you
6. Performetric
7. Unbabel
8. Veniam
9. Peekmed
10. Chic by Choice

3.2.1 Aptoide

Founded in 2009 in Lisbon, Portugal, by Paulo Trezentos and Álvaro Pinto.

Aptoide is an application for smartphones, tablets and computers and likes to describe itself as a safe alternative to Google Play. It allows you to purchase and download other apps through a store, but also to create your own store on the app to present your own apps. In 2015, Aptoide expanded her company in Asia by opening offices in Singapore and Shenzhen. Her future plans are to aggressively expand in Southern China, where, according to Aptoide, most OEM's are located as well as the low-end market of South East Asia. "With Google Play not available in China, there are many, many different app stores emerging there – local app stores" says Álvaro Pinto. "We are available there but due to the fierce competition, we are not popular in China on the B2B side".



Aptoide is one of the few companies that took part in the investigation that had already aimed for the Chinese market and was successful. Their website has a Chinese translation and their product is,

regardless of severe competition, highly popular in China.

Figure 6 – Aptoide logo, 2017; Source Aptoide

Aptoide has a WFOE structure and asked guidance of a consultancy group when entering the Chinese market.

3.2.2 Farfetch

Farfetch, is a Unicorn company from CEO José Neves, which founded 25 boutiques in 2007 to 2008. Their concept is Luxury Fashion, while offering brick-and-mortar boutiques a global reach and competitive technology solutions. In 2007 to 2008, already 25 boutiques of Farfetch were launched. In 2016 the company raised 66 million to grow in the US, Asia and Brazil. They have a Chinese partner ID6 Capital (founded by Richard Chen) and in 2017 resulted in China being one of their three largest markets so far.



The main question is: how does Farfetch look up on their collaboration with China? Do they come along any struggles while entering this Asian market? Is it very different from the US market and do they have any guidance while doing so?

Farfetch has an international website with Chinese translation and web shop as well. They entered the Chinese market as a WFOE and have asked the guidance of a consultancy group.

Figure 7 – Farfetch Online Store logo, 2017; Source: Farfetch

3.2.3 Feedzai

Founded in Portugal, the founders Nuno Sebastião, Paulo Marques and Pedro Biarro took the company right away to San Mateo, California in the United States: Silicon Valley. The product was created by data scientists and aerospace engineers. Feedzai is Citigroup-backed and a powerful AI tool, fighting e-commerce fraud and protecting merchants and their customers against cyber-attacks.



The launch, in Portugal, was in 2011 and it got a 2 million funding, making Feedzai to expand to the US market in 2013, opening an office in Silicon Valley and opening another office in the UK in 2016. Their future plans are to open an office in Asia. I would like to know if this also includes an office in China and if they have thought about on how to approach this market.

Figure 8 – Feedzai Arrow logo, 2017; Source: Feedzai

Feedzai is indeed interested in the Chinese market and is looking for extension for next year, 2018. They intend to go as a WFOE and are now in conversation with a few Consultancy Agencies in order to orientate better.

3.2.4 Findster

Findster also has Portuguese origins but was taken right after launch to San Francisco, California in the United States of America. David Barroso, Paulo Fonseca, Márcio Colunas and David Dieteren were the original founders from Findster that launched in 2013. The product is for tracking pets and kids. A GPS driven pet tracker without monthly fees or data charges, with stable coverage and it rewards its users for keeping their furry companions healthy. Their manufacturing is in Marinha Grande, Portugal and they intend to keep it there. They aspire to be available worldwide and I was wondering if this also included to be available in China.



Contact has been made with the International Relations department of Findster and after speaking with Jane Jonson, it got clear that they do not aspire to enter the Chinese market as their product is not yet relevant for the Chinese target audience.

Figure 9 – Findster logo, 2017; Source: Findster.com

3.2.5 Science4you

Science4you started as a project for the University of Lisbon, by Miguel Pina Martins in 2007. The university invested 50.000 Euros and since then, Science4you has grown into a big business with selling points in several European countries. Science4you is a product that produces applications, puzzles and other toys that help kids learn anything from science of slime to the basics of DNA. Their products are categorized by age, starting from 6 years old. They have collaborated with Discovery Channel and the University of Oxford and all Science4you toys remain being manufactured in Portugal. Since their start of 2007, Science4you expanded their market to Spain, Angola, Brazil, UK, Poland, France, Belgium, The Netherlands and Luxemburg and has Representative offices in Spain and the UK.



After speaking with Sebastião Lorena, Head of Marketing and Corporate Sales, it got clear that at the moment Science4you only has a contract with some distributors in China that have exclusivity to sell their product in China. This is a contract for 2 years and started in 2015. It works well but they do have issues, mainly on the language area: only a few speak English, so things get

lost in translation sometimes.

Figure 10 – Science4you logo, 2017; Source: Science4you

All of this taken in consideration, their main focus at the moment does not lie in the Chinese market. They do have sales in Singapore and Vietnam, but also the Japanese market and South Korean market for example are too specific to enter

without thorough preparation. Keeping their products being manufactured in their own country while 90% of the toys worldwide are produced in China, might have to do with their choice of not starting a Joint Venture or Representative Office.

Every year, Science4you presents its products on fairs in England and Honk Kong and every year in April their new business plans for the upcoming years are being internally negotiated. It is a possibility that China appears on their future plans for the company but that is now, in October 2017, too unsure to tell.

3.2.6 Performetric

Launched in August 2015 by André Pimenta, Serafim Pinto, Alaide Olambiwonnu and Davide Carneiro. He founders brought their product that is an application that avoids employee burnout and increases productivity with real-time fatigue management solutions, right after the foundation to Silicon Valley to attract customers. The application promises to be a solution for the current workplace fatigue that costs US businesses up to €136 billion yearly in production loss. In 2016 it attended the Web summit and in 2017 Performetric became available to more than 20 thousand talk desk users across 50 countries.



Figure 11 – Performetric logo, 2015; Source: Performetric

Performetric is one of the companies that was so kind to fill in the questionnaire without being certain of entering the Chinese market this upcoming year. However, they were interested in more information and I could inform them a little about the different types of investment vehicles and the Chinese customs that might become a challenge. They intend to get a consultant company that can help them further when deciding bringing their product to China.

3.2.7 Unbabel

A world without language barriers: harnessing AL and its global network of human editors, Y combinatory-backed, Unbabel is a multi-lingual translation engine for companies at scale. With this idea the 5 founders of Unbabel: Vasco Pedro, João Graça, Sofia Pessanha, Bruno Prezado Silva and Hugo Silva founded their e-commerce translation product in 2013. Today, in 2017, Unbabel already counts 40 thousand human editors and over 28 thousand language supporters. With head offices in Lisbon and San Francisco and clients including Pinterest, Trello, Skyscaneer, Zendesk and Salesforce, it is not a surprise that their estimated growth



Figure 12 – Unbabel Editor Sign-in, 2017; Source: Unbabel

They are considering, due to this growth, to open a third office in London or Asia. They were contacted for this Thisis to know if they are considering China and if so, why.

Unbabel will start negotiating bringing their company to China. They are still in the beginning of this process and asked for more information about WFOE's, JV's and RO's. They will most probably take a consultancy group in arms as they know very little about Guanxi and have heard of other companies that entering the Chinese market can be quite challenging.

3.2.8 Veniam

Founded in Porto, Portugal by João Barros, Roy Russel, Robin Chase and Susana Sargento in 2012. Veniam is a simple turnkey solution to turn moving vehicles into Wi-Fi hotspots, giving free, stable connectivity everywhere while collecting valuable data-bringing smart cities closer to reality. By the beginning of 2015 Veniam already had 110 thousand users a month in Porto only. Their first collaboration agreement was signed in November 2016 for Asia, Singapore. Their future plans are to venture to other Asian countries. I am making contact with this company to find out if they also intend to expand in China. And if this is not the case, then why not.



Figure 13 – Veniam – The Internet of Moving Things, 2017; Source: Veniam

Veniam did expand in China. This was one of their responses to the questionnaire, asking why they thought China was an interesting target for their product: “China has one sixth of the world's population. That is almost 15 per cent of all four plus wheeled vehicles and a telco spectrum approach which is fast paced. The significant number of mega cities (of more than 10 million people) and the government's drive for enhanced liability in those cities are all positive market signals. One final signal is the government's stated intent to improve intellectual property protection which is important for Veniam”.

Veniam has started to bring their company to the Chinese market. When a good product like this comes up, negotiation seems to go a lot easier. They have chosen the WFOE, as a company structure.

3.2.9 PeekMed

PeekMed, world's first 3D orthopedic software, lets surgeons reduce surgery time by up to 20% and increases accuracy, helping hospitals reduce sterilization costs by 50%. The idea for Peekmed was launched in 2015, in Braga, as part of a start-up with a funding from Portugal Ventures. The software is now used by 100 orthopedic doctors including doctors from Spain, Brazil, UK, US and India.



Is this product also used in China?

PeekMed is used in China but the company itself has not brought their company to China as a JV yet. First they will explore the market further, with help of a consulting group.

Figure 14 – Peekmed logo, 2017; Source: Peekmed

They were quite interested in more information and thought that knowing on how to bring your product to China and learn about Chinese customs and Guanxi first could be very helpful.

3.2.10 Chic by Choice

Founded in 2014 by Lara Vidreiro and Filipa Neto in Lisbon, Portugal. Chic by Choice is an online fashion store that lets costumers rent designer dresses in Vogue, straight from the catwalk - at 85% off retail prices. Practically right after founding Chic by Choice, he co-founders moved to London. In 2015 they closed a deal of 1,5 million euros investment. This money was used to expand in the UK and in Germany. Now, in 2017, Chic by Choice is available in more than 15 European markets including: UK, France, Italy and Germany. There future plans are to expand outside of Europe.



For this thesis' investigation it needs to be seen if the Chinese market is attractive for them and if they have China on their wish list when it comes to expanding their company.

Chic by Choice has made plans for extension in China and has considered both WFOE and JV as a company structure.

Figure 15 – Chic by Choice logo, 2017; Source: Chic by Choice

4. Results

In this chapter the results of the questionnaire taken by the 10 companies introduced in the previous chapter are discussed. All questions will be discussed separately, to get a good understanding of the differences and similarities of these 10 Portuguese start-up companies.

The first question is about the company's origin. Even though only start-up companies with Portuguese (co-) founders are asked, it needed to be made sure that all companies started in the same country and had the same starting point. Even though most participating companies almost immediately left Portugal and changed it for Silicon Valley or the UK, some have their manufacturing still in Portugal and keep close ties with the country of origin by keeping their first opened shop in Portugal.

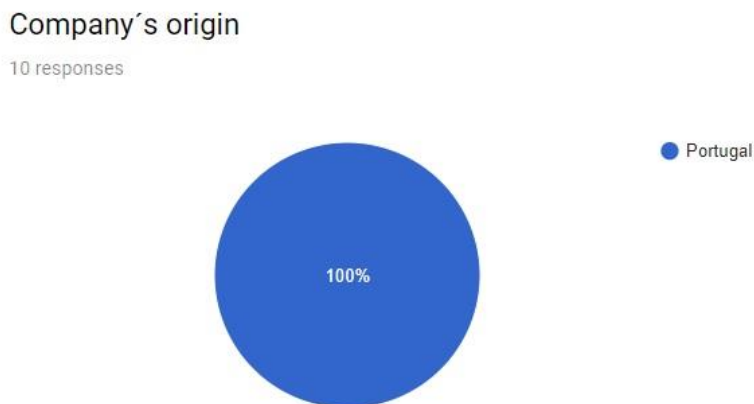


Figure 16 – Company's Origin, 2017. Source: Questionnaire for Student Research

The year of the launch of the companies interviewed, differentiated more. When starting to write this thesis, the intention was to only question Start-ups that had really just started. In 2015 until 2017. Later on, it became clear that even for a company to start in 2008, they still

are giving form to their business trying to set and sometimes modify their strategies and are most of the times overwhelmed of the success they booked in the short amount of time they exist. This is why the companies' origin had to be taken in a wider aspect. The result of this is that the eldest company interviewed inaugurated in 2004 and the most recent ones in 2015. All these companies are considered as Start-ups.

Year of launch

10 responses

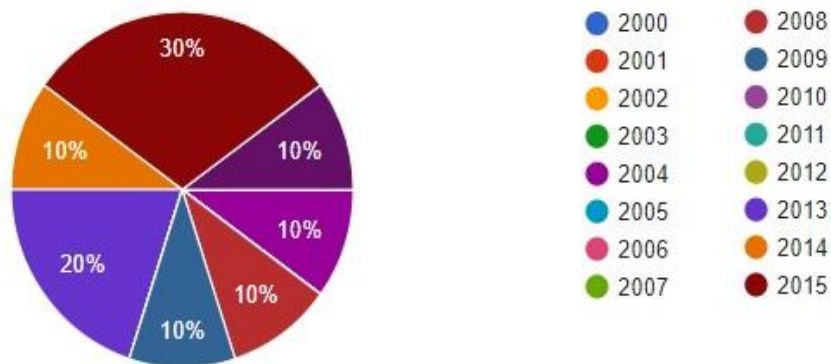


Figure 17 – Year of Launch, 2017. Source: Questionnaire for Student Research

After the given information about the company itself it seemed logical to ask the interviewees a general question about China. It is important to know how people look to China before and once they got to take their company there. The Answers given are some diverse and some quite similar. However, throughout all answers you can see that China is seen as a land of possibilities, chances and risks. Still quite unknown to most people and therefore also very challenging. Please take a look to the answers given by the 10 startup companies during the questionnaire:

How would you describe China in 3 words?

10 responses

Big, crowded, communist
Big, Copycat, cheap
Huge benevolent country
Relationships-driven Fast-moving Risk-taking
Innovative, endless possibilities
Open for different
Developing, unconventional, full-of-possibilities
Challenging, mass-innovative & result-orientated
Competitive land of possibilities
Risk-taking, innovative and challenging

Figure 18 – Describe China in 3 Words, 2017; Source: Questionnaire for Student Research

Of all companies interviewed, half of them were certain of wanting to enter the Chinese market, or taking their company to China. The companies that have answered “maybe”, did not have concrete plans, but did have China on their agenda for at the latest one year, it became clear after asking them to explain the motives of their answers better.

Have you made concrete plans about entering the Chinese market?

10 responses

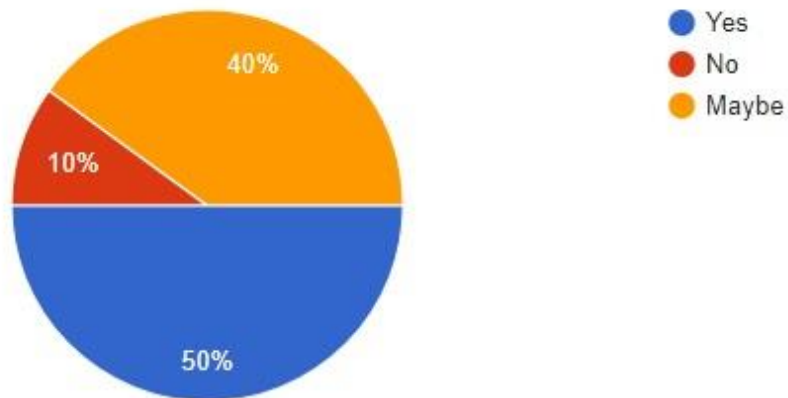


Figure 19 – Concrete Plans about Entering Chinese Market, 2017. Source: Questionnaire for Student Research

Only one of the interviewed companies is sure about not wanting to enter the Chinese market, yet. They kindly suggested to contact them again in February next year as all plans of the upcoming 3 years will be made and it could be possible for them to consider China after all. But at this point nothing is confirmed yet and only seen as a far possibility.

The follow up question of wanting to enter the Chinese market was “why would you choose this market”. It seemed to me as a logical question. Also, it was important to see if the answers given could be compared with the answers given before, when they are asked if they can describe China for me. Even though not all companies had answered yes to the previous question, all have considered China and based their answers on that. Please see image below.

If you choose "Yes" at the previous question, please explain why you chose to bring your business to the Chinese market.

10 responses

Possibilities to reach a large target group
n/a
China has 1/6 of the world's population- almost 15% of 4+ wheeled vehicles and a telco spectrum approach which is fast paced. The significant number of mega cities (>10m people) and the government's drive for enhanced livability in those cities are all positive market signals. One final signal is the government's stated intent to improve intellectual property protection which is important for Veniam
For our industry, B2B partnerships are mostly in China
Endless possibilities, larger market
We are considering, as it requires full attention
Challenging market, large requirement for our product
N/A
only in a few years
China's crazy drive for continuous development and innovation makes their market extremely challenging and attractive for young companies as ours, to explore possibilities.

Figure 20 – Why Bring Company to Chinese Market, 2017. Source: Questionnaire for Student Research

Practically all companies, as you can see in the image below, are informed about the different investment vehicles that are used in China. Most of the time, as a company, this part is already clear. However, some insight, regulation and further information from a consultancy group is very crucial as not all information found on the internet is complete or can be completely trusted.

Are you informed about the different types of investment vehicles (WFOE, JV, RO)?

10 responses

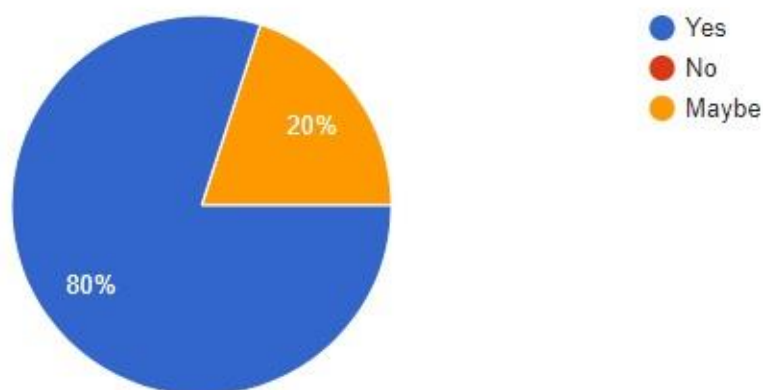


Figure 21 – Difference Investment Vehicles, 2017. Source: Questionnaire for Student Research

For a long time, Joint Venture has been the only type of investment vehicle that companies could choose when entering the Chinese market. This regulation has changed a few years ago and ever since, Wholly Foreign Owned Enterprises are the most chosen vehicle.

If you answered "Yes" at the previous question, please fill in below what type of investment vehicle you think would suit your company best.

10 responses

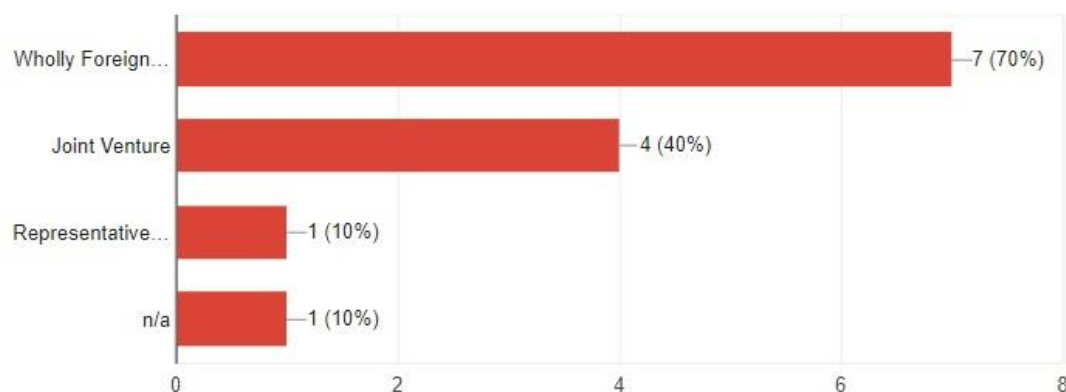


Figure 22 – Which Investment Vehicle Chosen, 2017. Source: Questionnaire for Student Research

The reason of choosing a certain type of structure has been discussed throughout this thesis. It will be really interesting to also hear the thoughts and opinions of the companies interviewed and therefore it would be a logical next question on the questionnaire to ask them about their thoughts. Please see image below for the responses. The majority of companies interviewed and also the majority of companies in general, choose for WFOE as they would like to keep “full control” over their product and services. Still China is seen as a smart country that can cause you to lose your patent on product and make profit out of shared ideas.

Can you explain why you chose this type of investment vehicle?

10 responses

I'd like to keep full control
n/a
Access to Contacts and local ownership is important for market acceptance
We don't have revenue through CN, only expenses so the limited and easier bureaucracy / taxing is a plus
Would like to keep full control
Would like to stay in charge
We would like a joint collaboration but at the same time not lose our patent on ur products
WFOE has been recommended to companies that wish to keep full control and do not want to give any knowledge about their product out of hands.
Still deciding
Less risks of product exchange when completely in charge

Figure 23 – Reason of Choice Investment Vehicle, 2017. Source: Questionnaire for Student Research

Before entering the Chinese market, companies are informed by other companies' experiences. This can both be positive or negative. How do these companies deal with this information? What kind of feedback will they get and how much influence has this? Experiences of other companies will not were hold these companies of entering the market but will maybe give them ideas and they will react from that. Peter Pronk from 1421 already said that in order to be fully prepared you have to expect nothing, expect the unexpected. Please see image below for the results.

Before entering the Chinese market, have you heard reviews from other companies about negotiation with the Chinese people?

10 responses

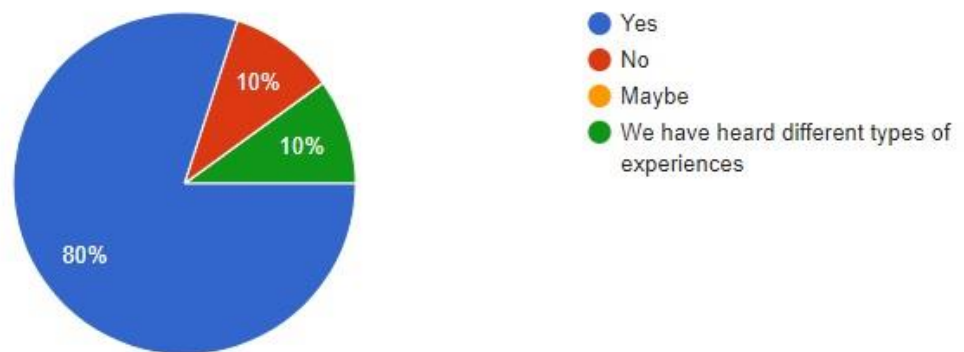


Figure 24 – Other Reviews Heard, 2017. Source: Questionnaire for Student Research

At the graphic below you can see that practically all companies have considered a consultancy company to help them or already taken one in hand. Consultancy companies like 1421 Consultancy Group are a great asset for a new company trying to enter the Chinese market. No European company, especially startups, are recommended to enter the Chinese market without a proper consultancy agency.

Have you considered hiring a qualified company that can help you with legal matters and can inform you about the procedures of entering the Chinese market?

10 responses

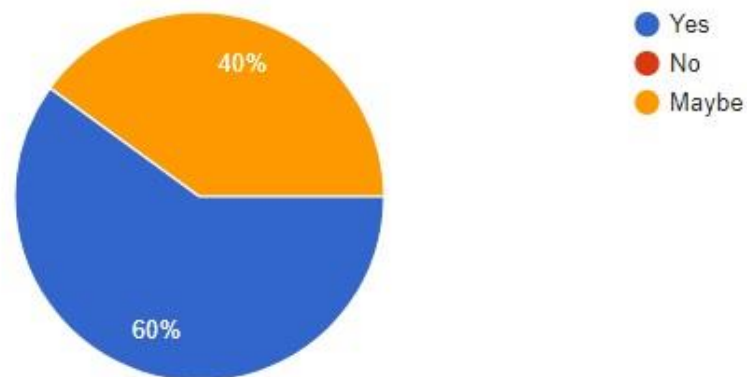


Figure 25 – Hiring Consultancy Company, 2017. Source: Questionnaire for Student Research

The last, but not less important question, is about Guanxi. Relationships. As throughout this thesis is concluded that Guanxi is definitely important for Chinese and thus for companies negotiating. Knowing what this means might bring Western startups closer to what it means to negotiate with Chinese companies and actually succeed in coming to an agreement that is satisfactory for both parties.

Are you familiar with the term "Guanxi"?

10 responses

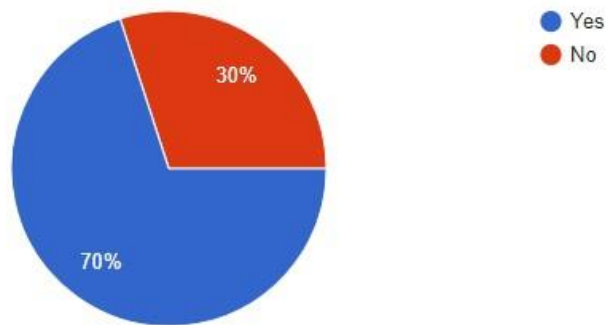


Figure 26 – Guanxi, 2017. Source: Questionnaire for Student Research

5. Conclusion

Throughout this thesis we have seen what company structures you can choose when entering the Chinese market. How to negotiate and make contact with Chinese partners and associates and how to deal with difficulties during this process. Based on the results of the questionnaire, the conversations held had with the companies, consultancy groups and information that has been collected, my thoughts are as follows.

Starting a company in China, the steps:

I. Do your homework.

Talk to people who have opened offices in China. Ask them how they succeeded and especially how they failed. Contact a consultancy agency and travel to China and start networking at local trade shows, as relationships are crucial to doing business in the country.

Make sure you're informed about the state of the industry that you are dealing with. This research does not necessarily have to be in China but can be done from home. Check out the five-year plan that the Chinese government publishes, which details what types of businesses they're looking for. Last Communist Party Conference was held in October from this year.

China want businesses that will give a lot of people good jobs, and they want to encourage development inland. Because China's government is so tightly affiliated with its businesses, knowing what the government wants will help you draft your business plan later on.

II. Pick a location.

Even though you have a whole country at your disposal, it is better to first get to know the big cities. Shanghai, Beijing and Guangzhou, Shenzhen and Chengdu are the major business, government, and industrial centers. The very nature of your business may require you set down in one of the big cities. If you're a tech company, for instance, Beijing may be the place for you. Find out where the action is happening in your industry.



Figure 27 – Map of China Industries, 2009. Source: Gifex

The major business centers aren't your only options. Some companies find moving inland to be the better bet. Ask yourself the following questions, especially if you're selling goods rather than services, to determine how near to or far from the coast you need to be:

- What are your transportation needs?
- What are your logistical needs?
- Are you relying on goods that may be imported to China?

- iv. How can you get the goods from the port to your location?
- v. What government inspections and restrictions will you be subject to?

Once you've settled on a region, you have to find an office, since you'll need proof of a lease to register your business.

Whatever space you choose, make sure it is zoned for the type of business you're planning on opening.

III. Choose your investment vehicle

Before you register with the government, you need to decide what type of investment vehicle to register. All investment vehicles are described throughout this thesis. Choose well on the given information and decide if you go for a *Wholly Foreign Owned Enterprise (WFOE)*, *Joint Venture (JV)* or *Representative Office (RO)*.

Starting a Joint Venture Enterprise in China, the steps:

Stage 1: Preliminary approval - Project Proposal

Upon reaching a mutual agreement, the Chinese partner will be solely responsible for the preparation and submission of the project proposal for preliminary scrutiny.

Generally, the authority will give an official reply within 20 days upon receipt of the proposal and other relevant documents. An approval or rejection letter will be issued to the applicant. The foreign party in a JV should request a copy of this document from the Chinese partner to ensure that the approval is consistent with the agreed terms of the project.

Upon receiving approval, the Chinese partner will proceed to register the name of the enterprise with the local Administration for Industry and Commerce (AIC).

The application will require basic facts about the project, information about the technological and technical processes, demand on energy and other resources, an assessment on possible environmental impact, prices of public goods or services involved, the means of capital contribution and financing, and a list of the equipment to be imported and the amounts required.

The relevant documents for submission include enterprise registration certificates of the Chinese and foreign investors, credit certificates, letter of investment intent, and an environmental impact assessment report issued by the environmental protection administration.

Stage 2: Formal approval - Contracts, Articles of Association

The contract, articles of association and other relevant legal documents for establishing the JV will be signed by both parties and submitted by the Chinese partner to the provincial or municipal Ministry of Commerce for approval. After the contract and articles of association are approved, the same partner would proceed to apply to the provincial or municipal Ministry of Commerce for an approval certificate. Chinese law views the joint venture contract as the fundamental document for the establishment of the venture. The contract must meet the conditions stated in China's joint venture law (for equity JVs) or cooperative enterprise law (for cooperative JVs). The preliminary project approval documents are included as appendices when the contract is submitted for formal approval.

The documents required include the application letter for establishing the JVs, a feasibility study report (if any) and approval documents for the project, an application for registration of the name of the enterprise with approval from the provincial or municipal AIC, written comments on the project by various government departments such as environmental protection, fire services, health and land administration, business licenses of the parties concerned and certificates of their legal representatives, contract and articles of association duly signed by the legal representatives of the JV parties, and the list of Board of Directors.

Stage 3: Business License

JVs should register with the local AIC and apply for a business license within 30 days upon receipt of the approval certificate. The local AIC will then issue the business license within 10 working days to projects that have passed the examination. The date the business license is issued will be considered the official date of the enterprise's establishment.

Having acquired the business license, the JV has to finish up with procedures such as applying for an official seal and enterprise code, opening a bank account, and registering for tax payment and customs declaration with the local public security, technical supervision, taxation, customs, finance, foreign exchange administration, banking, insurance and commodity inspection departments.

Starting a Wholly Foreign Owned Enterprise in China, the steps:

Stage 1: Preliminary approval - Project Proposal

The application procedure for setting up a WFOE is simpler. The project proposal will be prepared by the foreign investors and submitted directly to local authorities. The foreign investor may appoint a local agent to liaise with the government. To do so, he has to sign an authorization letter stipulating the agent's scope of services, responsibility and fees.

Generally, the authority will give an official reply within 30 days upon receipt of the proposal and other relevant documents. The approval or rejection letter will be issued to the foreign investor. If a favorable reply is received, the foreign investor can proceed to register the company's name at the local AIC.

The report must contain information regarding the objectives of the WFOE, business scope, scale of operation, products to be produced, technology and equipment to be used, land area required, conditions and quantities of water, electricity, gas and other forms of energy resources required, and requirements for public facilities.

Stage 2: Formal approval - Articles of Association

After the foreign investor receives a written reply from the relevant government authorities, a formal application supported by all the required documents should be filed with the local Ministry of Commerce at a county, municipal or provincial level. After receiving the formal approval, the foreign investor should apply to the Ministry of Commerce again for an approval certificate by presenting all the necessary documents.

The required documents include the application letter for establishing the WFOE; a feasibility study report (if any), articles of association, list of legal representatives (or Board of Directors), the foreign investor's legal papers and credit report, a list of materials to be imported, written replies from the local approval authorities at county level or above, application for registration of the name of the enterprise approved by the provincial or municipal administration AIC, comments on the project by various government departments such as environmental protection, fire services, health and land

administration. In the case where two or more foreign investors are involved, copies of the contracts signed by them should be submitted to the approval authority for their records.

Stage 3: Business License

Upon collection of the approval certificate, an application for a business license has to be filed with the provincial or municipal AIC within 30 days. The local AIC will issue the business license within 10 working days to projects that have passed the examination. Likewise, the date the business license is issued will be considered the official date of the establishment of the enterprise.

Having acquired the business license, the WFOE has to finish up with procedures such as applying for an official seal and enterprise code, opening a bank account, and registering for tax payment and customs declaration with the local public security, technical supervision, taxation, customs, finance, foreign exchange administration, banking, insurance and commodity inspection departments.

Starting a Representative Office in China, the steps:

A representative office may only engage in non-profit making activities. Accordingly, it may engage in any of the following functions: conducting research and providing data and promotion materials to potential clients and partners, conducting research and surveying for its parent company in the local market, liaising with local and foreign contacts in China on behalf of its parent company, acting as a coordinator for the parent company's activities in China, making travel arrangements for parent company representatives and potential Chinese clients and other non-profit making business activities.

Stage 1: Appoint an Agent

The applicant appoints an agent, which must be a Foreign Enterprises Service Company or "FESCO" in Mainland China. The local agent must be authorized by Ministry of Commerce of the PRC to handle representative office applications.

Stage 2: Submission of Applications

On behalf of the applicant, the Chinese agent will submit all the required documents to the provincial Ministry of Commerce for the handling of application procedures.

The relevant documents include the application letter signed by the Chairman of the Board or General Manager; incorporation documents of the company, the previous year's financial statement; an original bank reference letter attesting to the company's financial status, a letter of appointment of the chief representative signed by the Chairman of Board or the General Manager with the company's stamp and the chief representative's resume, copies of his or her identification, passport and photos, and a copy of the leasing agreement for the representative office and other documents that are requested by the authorities.

Stage 3: Business Certificate

After obtaining an approval permit from the provincial or municipal Ministry of Commerce, the foreign investor should proceed promptly to the provincial or municipal AIC for registration and acquire a business certificate.

Stage 4: Post-registration formalities

Other formalities to be handled by the resident representative:

Complete residence application procedures with local public security bureau by presenting the registration certificate, representative certificate and approval certificate.

Apply to open a bank account by presenting registration certificate and approval certificate to local foreign exchange administration.

Apply to Customs for permission to import office equipment, daily necessities and transport vehicles for use by the representative office and its personnel.

Complete tax payment registration procedure at local tax office.

IV. Develop a business plan.

A detailed five-year business plan is crucial, because once the government approves it, you will be able to operate only within its guidelines. If you start offering a product or service that is not in your business plan, the Chinese government can shut your business down. The same goes for where and how you operate.

Michael Pronk from 1421 Consultancy Group recommends to make sure your business plan is as broad as possible to allow the company to operate freely, foreign companies often expect to operate in a certain way here and they realize their business license may not allow them to do that. While it needs to be broad, it should also be specific. Make sure you include your location, projected revenues, product or service description, expected number of employees and budget requirements in the plan.

V. Find a Consultant Agency

No matter how informed you are, you won't get very far without consulting a representative to register your business. Organizations like 1421 Consultancy Group can help you navigate the complicated application process. Consult the Portuguese Chamber of Commerce or one of the acknowledged consultancy groups. All of these resources should be able to recommend a trustworthy international corporate lawyer for you. A qualified liaison should be able to tell you where you need to go to register, whether it's the local, provincial or national government, and should do the talking once you get there.

VI. Organize the necessary documents.

When hiring your Consultancy Agency, they can help you with all these steps. However, there is still the written laws in China against the reality on the ground. This theory especially applies when it comes to what documents you'll need to register.

Local authorities can say they want to see exactly what it will be you are manufacturing. Application forms may also differ depending on who you're dealing with, so it's usually best to get it directly from the local authority.

VII. Trademark your intellectual property.

Intellectual property violations are a big issue for foreign investors in China. Often Foreign manufacturers believe that because they have a trademark at home, it will hold up in China,

but that's not the case. In China, the first person to register a trademark owns the rights to it, regardless of whether or not that person is the first person to use the trademark.

Patent

Applications for patent registration are handled in accordance with China's Patent Law and the Implementing Regulations of the Patent.

For patents on inventions, early announcement of the application can be made upon request. For utility model and design patents, examination is only carried out as a form of formality.

The State Intellectual Property Office is responsible for handling and examining patent applications and granting patent rights in accordance with the law nationwide.

FIEs applying for patents can either submit their applications directly or appoint designated patent agents. Due to the technical complexity involved in patent application, FIEs are advised to appoint agents in order to better protect their rights. Foreign enterprises applying for patents in China are encouraged to choose agents authorized by the State Intellectual Property Office to deal with foreign applications.

Protection of Intellectual Property Rights

To provide effective protection for foreign investors, Chinese government has come up with new regulations to improve its intellectual property system over the past few years.

China's intellectual property legislation stipulates that infringement of intellectual property rights (IPRs) will be dealt with by administrative procedures and legal proceedings.

In terms of civil liabilities, the infringer may be ordered to stop the act, eradicate the damage done, make public apologies or compensate for damages. In terms of administrative measures and criminal liabilities, warnings and orders to stop the infringing act will be issued. There is possible confiscation of unlawful gains, fines, and demands for damage compensation.

When an IPR infringement dispute arises, the parties may choose to opt for mediation. If mediation is not preferred or fails, or if one of the parties involved refuses to abide by the outcome of mediation, legal proceedings may be instituted with the people's court. The persons may also request for the relevant administrative authorities to take action.

VIII. Find a bank.

This part should be quick and easy, since there are plenty of banks with a huge presence in China. If you're dealing with a bank that doesn't have any relationship with banks in Portugal or other European Country, it might be harder to keep track of your money. You want to make sure you have a bank in Europe and a bank in China that has some sort of corresponding relationship, so your banking is more transparent.



Figure 28 – China Banks Global Branches, 2011. Source: CKGSB Knowledge

Top 5 Chinese banks by global branches:

Industrial and Commercial Bank of China – ICBC (中国工商银行)

Bank of China (中国银行)

China Construction Bank (中国建设银行)

Agricultural Bank of China (中国农业银行)

Bank of Communications (交通银行)

IX. Hire a staff.

Hiring in China is a delicate process, especially when it comes to hiring managers. The language skills can be greatly beneficial, but it's even more important to have a smart business person in that role who's going to run the company the way you want it run.

What can be a good strategy is to hire a Chinese public relations professional and let them come to the company's headquarters in Europe or Silicon Valley, to learn the ropes for several months. Then they will return to China with all the company's values and practices in mind starting the business. There are other options, like trying to reach out to human resources consultants and headhunting agencies in China. European or American-born Chinese or Chinese citizens who were schooled in America can also be a good asset. Once you have trusted managers in place, they should be able to assist you in hiring the rest of the staff. You will need to have a contract for every employee you hire, as well as an employee manual.

X. Have patience.

Now that you're all set up, you have to manage expectations. Things can move slowly in this fast-growing country. Something also most Consultancy groups tell us is: "If you don't leave your Western lens behind, it can be frustrating". It takes time to build business relationships in China.

What will win you success in the Chinese market is patience. "The Chinese have been doing business in a certain manner for thousands of years. Don't even start to think for a millisecond that you're going to change it."

And still, the most important, what companies tell throughout all conversations held with them, consultants, and specialists, is that it all starts with coming with a good product. When you

come with a product that can really benefit the Chinese market that they will see as an innovation and worth investing in, then you are already with one foot in and all that rests you is to have an open mind and a good sense of adventure. Good luck!

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7. Appendices

Letter written to 10 Portuguese startups:

Dear Sir, Madam,

My name is Eva van Lenteren and I am studying Chinese Studies at the University of Aveiro, Portugal. At the moment, I am writing my thesis as a part of these studies and I am investigating Portuguese Start-up companies who want to enter the Chinese market.

Through the website of Compass list, I got to learn a little bit more about your company Feedzai and I would like to know who, inside your company, I can approach and is willing to answer some of my questions about your plans to enter the Chinese market: if you are interested, which investment vehicle are you thinking about to choose? What are your expectations about taking your company to China? Etc.

As far as I can see on the Compass list website your company's future plans are to open an office in Asia. I would like to know how the progress of this expansion is going and if you came across any difficulties or obstacles so far.

Included to this email is a link to a questionnaire that will not take much of your time. I would appreciate it a lot if you could answer these questions for me.

Go to questionnaire:

[Link](#)

If you would have the time to tell me a bit more about your experiences, maybe through a Skype meeting or otherwise over email, that would be great.

I am looking forward to your reply.

Kind regards,

Eva van Lenteren